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The Bank is not necessarily in agreement with the views expressed in articles appearing in this Review. They are published in order to stimulate free discussion and full inquiry.

Notes on Public Finance

By Lionel Robbins

I

INTRODUCTION

THE following notes on certain very general aspects of the problems of public finance are not specifically related to the more technical details of our present budgetary position. In so far, however, as the accession to power of a new government is a moment when the wider implications of policy may be legitimately conceived as due for consideration, they may perhaps be thought to have some practical relevance. That, at any rate, is their intention. I have the feeling that we are apt to take for granted certain tendencies of contemporary financial policy and to dismiss the prospect of any substantial change as impracticable. My main object is to show that this attitude is uncalled for.

II

THE IMPORTANCE OF PUBLIC FINANCE

The first point I want to make is the importance of public finance.

By this I do not mean merely the importance which has been traditionally associated with it for constitutional or personal reasons. Needless to say, the provision and expenditure of public money is a matter of great constitutional significance; and anything which affects our pockets on the scale on which they are affected by modern taxation is a matter of great personal concern. What I have in mind much more in this connection is the positive rôle which is played by the system of public finance in the general working of the economy.

This shows itself in two ways. We are gradually getting used to the idea of the budget as an instrument of over-all stabilization. If the economy is tending to depression we look to measures of public finance to help to reverse the tendency; if it is tending to boom we look for some fiscal curb. It is greatly to be hoped that the revival of monetary policy, which had been so foolishly neglected in the years immediately after the war, will not lead us to abandon these expectations. It is perhaps possible to imagine a world in which the business of

stabilization could be left entirely to monetary measures. But the world we inhabit, with its rigidities and insensitive spots, demands a more eclectic treatment. The need for the use of the budget as a stabilizer is a need which has come to stay.

But beyond this we have to take account of public finance as an influence on the long-term evolution of the economy. By this I do not mean merely the use of public funds to finance particular industrial schemes or to encourage particular developments. Doubtless that plays a part—and in some countries an important part. I mean rather something much more far-reaching than this : I mean the general influence of the system of public finance on enterprise, accumulation and the distribution of income and property.

In a vague way, of course, we acknowledge this influence. We spend a great deal of time discussing the influence of taxation on enterprise—with singularly little result. But do we sufficiently appreciate the much more tangible influence of taxation on general social and economic structure? Do we fully realize the way in which the appearances of the material and social world are changed and moulded by the influence of public finance? It is doubtful.

Yet if we consider what actually happens this influence is very obvious. Any man over fifty, who pauses to reflect, knows at once that the world of today is changed almost beyond belief from the world in which he grew up as a boy—the look of town and country, the way we live, the texture of social relations, the distribution of influence and power. Some of this is due to technique—the automobile, the aeroplane, the radio—some to the general growth of wealth and population, some to the shattering impact of war. But any attempt to enumerate the main formative influences which left out the influence of taxation and its effects on relative demand would be very incomplete. In the sphere of policy, indeed, the influence of the tax system is probably greater and more continuous than any other.

We can see this very vividly if we consider alternative forms of policy. In the politics of recent years, the intention to produce change has been quite deliberate. We have had various kinds of control. We have had widespread measures of nationalization. Yet compared with the relentless, ubiquitous influence of the tax machine, these things sink into insignificance. I would not argue that it is a matter of indifference whether certain industries are, or are not, collectively owned and

managed ; the disadvantages of a form of industrial organization which seems at once insusceptible to control by other organs of the State and yet a continuous liability to the Exchequer if anything goes wrong, seem to me to be not inconsiderable. Yet the difference which is made to the distribution of wealth and to social relations generally by, for example, the replacement of the old marks "G.W.R.", "L.N.E.R.", etc., by the omnibus "British Railways", counts for very little compared to the operation of death duties and income tax. In the revolution of our time it is the tax machine which is the principal revolutionary agent.

If I were asked to sum up in a word the salient characteristic of this revolution, I should choose the word collectivism. "We are all socialists now", said Sir William Harcourt, when he introduced the death duty principle ; and he spoke better than he knew. There are naturally many other ways of conceiving the changes : the equalization of income is an important aspect, of which there will be more to say later. But in the end, I think, it is the collectivist tendency which is dominant : the tendency to shift more and more the sources of initiative to the central government and its organs. Even the equalizing tendency, as it works under the present system, has chiefly this significance. True, it redistributes income ; but it also destroys independent sources of power. It leaves more to be done by government.

Now let me say at once that I do not think that all aspects of this tendency are bad. Up to a point I have no objection to Sir William Harcourt's description. Many of the extensions of the functions of the State which we have witnessed in our time seem to me to be necessary and desirable, in particular all those which serve positively to create greater equality of opportunity. But ideally I would wish these extensions to take place in a *milieu* in which there were sufficient checks and balances to prevent them becoming predominant, so that although the *absolute* area of state activity had increased, it had not increased *relatively*. But, of course, the collectivism of this country in this day and age has not been of this nature. While, thank heaven, we are still far from the limiting condition in which there is only one property owner and one employer, we have gone some way along that road. There can be no doubt that the power of the State, relatively to other social elements, has greatly increased. And this seems very much to be regretted.

How far is this to be regarded as inevitable? To what

extent are the influences which have brought it about to be regarded as inescapable? It is to the exploration of these questions that the main body of this inquiry is directed.

The arrangement dictates itself. The influences with which we are concerned spring, partly, from the sheer weight of taxation, partly from the peculiar nature of the tax structure. It will be convenient to follow this order.

III
THE WEIGHT OF TAXATION

To begin then with the weight of taxation.

It would be wrong to say that this is the cause of all the trouble; it will be one of the main contentions of these notes that, given the *amount* to be raised, it makes a great deal of difference *how* it is raised—that the nature of the tax structure is very important indeed. But it is nevertheless true that, if the amount were less, differences of structure would also be less important. In this sense, it is right to regard a good many of our difficulties as springing from the large amounts, in relation to the totals of national income, which the tax system is called upon to provide. Certainly, a good many of the problems with which the beautifully written Report of the *Royal Commission on the Taxation of Profits and Income* is concerned would diminish greatly in significance were it possible for us to return even to immediately pre-war proportions of public expenditure.

What are the hopes of reducing this burden?

To get our ideas straight on this very vital question, it is essential to clear our minds of *clichés* and wishful thinking. There are still a great many people who lift up their voices in public who are under the impression—or who at any rate succeed in creating the impression—that there are vast easements to be secured by some general process of what they call " economy ". If only some great Chancellor would arise, they seem to argue, who would nerve himself to exhort a spendthrift and complacent bureaucracy to *"cut out the waste"*, all would be well; and, alas for the vanity of human wishes, Chancellor after Chancellor disappoints them.

Now we must not quarrel about words in this connection. Doubtless there are senses of the words " economy " and " waste " which would oblige us to treat such exhortations with respect. In so far as we are spending more than we can easily bear, the situation may be said to call for economy. In so far as the money which is spent one way, could more profitably

be spent some other way, the expenditure may well be described as wasteful. There is undoubtedly much need for economy and much money wasted in these senses.

But if these words are taken to refer, as the context usually implies, not to broad questions of policy but to the costs of administration, it is safe to say that they are empty and misleading. There are no economies conceivable, there are no wastes in the sphere of administration, whose achievement or elimination would affect very substantially the present problem of the dead weight of taxation.

In saying this I do not mean to say that all administration is " economical ", that there are no examples of " waste " anywhere in the system. That would be absurd. I am sure that bad patches exist and that there is always room for improvement. What I mean is simply this, that the costs of the administrative machine are so small in relation to the other objects of expenditure that to focus attention on them, rather than on the costs which are the result of policy, is to get the picture totally out of perspective.

Consider, for instance, the vote of the Ministry of Agriculture and Food. The aggregate amount for the current year is over £300 millions, of which no more than £16 millions are the costs of the machine, the rest being accounted for mainly by subsidies. Thus, if all the administration could be done for nothing, or by the Minister himself and a couple of secretaries, we should still be left with expenditure which is 95 per cent. of the present vote.

There are indeed real problems of economy and real problems of cutting out waste—problems which involve sums which are really appreciable in relation to the total volume of expenditure. But these problems arise, not in the sphere of administration but in the sphere of policy, a sphere for which the much-abused race of administrators has no responsibility. Nothing could be more conducive to cynicism than the spectacle of members of Parliament working themselves into a fury of righteous indignation about some delinquency of administrators, involving perhaps a few thousands and then, sheeplike, trooping into the lobbies to endorse policies which involve the expenditure of many millions.

What, then, are the prospects of economies in the sphere of policy?

Here to get a sense of proportion it is desirable to divide the problem into broad sections.

Clearly there can be no question of reduction in the matter of War Pensions or interest on the National Debt.

Defence expenditure is obviously reducible. But it is profoundly to be hoped that, until there are much more tangible signs of a will to peace elsewhere than have yet been forthcoming, there will be no relaxing here. The enormous expenditure under this head is, of course, one of the main reasons for the change in the proportion of public expenditure to national income since the inter-war period. But since it is this expenditure which hitherto has helped to save us from the fate of the Iron Curtain satellites, it is surely a part of the burden which should be borne without complaining.

There remains, therefore, the sphere of expenditure on domestic objects. Here there is an area of statutory benefits in respect of some kinds of social insurance which presumably is to be regarded as politically—and, I would say, ethically—inviolable. Beyond this, as Mr. Gaitskell showed with his token scheme of a shilling for prescriptions, there is a certain room for manœuvre, even in regard to welfare expenditure; and in the sphere of subsidies, there is a very appreciable margin indeed. I wonder whether many people whose pockets are not immediately affected really believe that the present volume and objects of agricultural subsidies make any kind of economic sense.

Nevertheless, politics and vested interests being what they are, a man would be sanguine indeed who would venture to predict any very substantial lightening of the burden from deliberate reductions of policy. Of the scope for such lightening there can be no doubt. But it is only in the shadow of dire catastrophe that we should be likely to do it on any very extensive scale.

Much more hopeful in the long run is the easement which may come with a gradual increase in the volume of production. If production increases at a modest rate, and if on balance we do not increase our present commitments, then a quite substantial shift in the proportionate burden might be expected. In this connection, I would like to draw attention to a very interesting article which has recently appeared in the *District Bank Review*, from the pen of Mr. Alan Peacock. In this article Mr. Peacock shows that, on the assumption of an increase of production of two per cent. per annum, even if we make an allowance for the increase in social expenditure at present rates due to increases of population, or changes in age composition,

by 1964 government expenditure as a percentage of gross national product could have fallen from the 34 per cent. of 1953 to 29 per cent., and by 1979 to 22 per cent.

These are very substantial reductions and the rate of increase of production assumed is very cautious. But the underlying assumption is critical: namely, that we do not change the real rates of present commitments. Over the years, a substantial easement is attainable without any positive cuts; all that is necessary is to mark time where we are, not to increase the rate of commitment in one line unless it can be diminished commensurately in another. This is not very much to ask. But whether this degree of self-restraint can be expected of future governments is anybody's guess. Personally, I should be very unwilling indeed to bet heavily on no net increase. But I should be disagreeably surprised if what increase there is should be so large as to wipe out the whole of the possible relief.

IV

THE PRINCIPLES AND PRACTICE OF PROGRESSION

Any relief of this sort, however, lies some way ahead in the future. At present, failing reductions in expenditure due to major changes of policy, any hope of making the tax system work in a less collectivist direction lies in changes in the tax structure.

Let us look at this, first, in regard to the taxation of income.

From the point of view of these notes, an inquiry into long-run social and economic effects, the salient feature of our income tax is its high rate of progression.

Now it seems to be commonly accepted nowadays that there should be some degree of progressiveness in the tax system. Why there should be this agreement is not altogether easy to see. The argument for the kind of progression which arises from the mere fact of an exemption limit is, of course, very plain: even the most strenuous supporters of the principle of proportionate taxation have been willing to concede that their principle should not come into operation until a minimum of subsistence had been provided for.

But, beyond this, the grounds for agreement that, as income increases, it should be taxed more than proportionately, are not at all obvious. It is all too plain that the principle of progression necessarily involves very awkward anomalies; the grievous

position of authors, artists and others with highly fluctuating incomes is a case in point. And the intellectual arguments which are usually cited in its favour are, to put it very mildly indeed, by no means unequivocal—the famous application of the minimum sacrifice principle is surely the hedonistic calculus at its most unconvincing.[1] Nevertheless, most of us—including the present writer—do agree in a vague and woolly way that some degree of progression is desirable—and it would be otiose to argue over-much here with this particular manifestation of the *Zeitgeist*.

But to agree that *some* degree of progressiveness is desirable does not involve agreement with *all* scales of progression. And I think that it is about time that someone who is not deeply involved personally, having chosen a different way of life, should say bluntly that the higher reaches of our own progression are quite indefensible save upon avowedly confiscatory theory. So far as earned income is involved, they constitute a discrimination against enterprise and ability such as has never before existed for any long time in any large-scale civilized community. Certainly they are not dictated by the needs of revenue: the upper rates of surtax could be just cancelled without creating any very severe budgetary problem. The most that can be said in their defence is that they were brought into existence at a time of crisis when they did not seem—and indeed were not—inappropriate to the needs of the situation and that, now that that crisis has passed, they have continued to exist because those who rule over us have been afraid to challenge the purely demagogic arguments by which they are usually supported.

Public criticism up to date has tended to be concentrated upon the effects of these rates on incentive. These are not effects whose significance I have any disposition to minimize. The arguments which do that have always seemed to me to be singularly futile. Of course, it is quite true that a substantial amount of the more conspicuous work of the world is done from non-pecuniary motives. It is true, too, that experience shows that

[1] If any reader, not being a fanatical egalitarian, should think that these sentiments are too sceptical, I should like to draw his attention to a remarkable essay, recently published by two members of the Chicago Law School—*The Uneasy Case for Progressive Taxation*, by Walter J. Blum and Harry Kalven, Jr. (University of Chicago Press). Messrs. Blum and Kalven have no axe to grind: their book is a perfectly dispassionate examination of a case, with no very clear conclusion emerging. But they certainly succeed in showing how extremely superficial has been most of the argument up to date on this extremely important question; and, incidentally, they show, too, how to conduct a very difficult economic and ethical investigation without becoming involved in jargon or obscurity.

when men in responsible jobs are remunerated by salaries which do not fluctuate with effort, a substantial proportion can be relied upon to do their work with competence and zeal—though there is also a proportion who do not. But to argue that, where income does fluctuate with effort and enterprise, there is no disincentive from high marginal rates, does not seem to me to make sense. If we would not argue that it made no difference if the marginal rate is 20s. in the pound, so that there was *no* reward for additional risk and effort, why should we contend that the position is so radically changed when the residue from a pound's worth of earnings was 6d. or 1s.?

But important as may be the incentive effects of extreme progression, they must surely take a second place beside the more general effects on economic and social structure. It is indeed a surprising circumstance that these are not more widely realized. We are told that under the present system, the number of *net* incomes (i.e. incomes after tax) over £6,000 a year is now less than two hundred; and the suggestion is that the revolution of which this is a symbol is to be regarded as an unequivocally good thing.

To me the verdict seems a much more difficult business. Perhaps this is due to some personal inhibition. But I must confess that the circumstance that it is now virtually impossible to build a fortune like Lord Nuffield's does not fill me with any particular enthusiasm. On the contrary, I can see several grounds for regarding it with some apprehension.

Is it a particularly good thing, I ask myself, that there should no longer be any substantial blocks of individual wealth whose owners can defy fashion, foster minority causes and give succour and support to the eccentric and the unpopular? Are we really very glad that in future so few private persons will be in a position to commission the building of architecturally pleasing dwellings of any considerable size or to support on a large scale independent institutes of learning? Do we regard it as a specially fortunate circumstance that benefactions of the kind which gave the nation the Courtauld pictures and the Courtauld Institute should, in future, be virtually out of the question; and that what support is given to the arts and culture, not to mention the universities, should have to come, if it comes at all, from central or local government? I am far from thinking that, in the old days, the provision made by the owners of private wealth for the general

cultural needs of the community was all that might have been wished; and that there was no need for supplementation by public money. Quite the contrary. But a situation in which there are no sources of initiative save at the centre seems to me at least as unsatisfactory as a situation in which the decentralized sources are inadequate.

But the consequences of levelling to this extent are not limited to the world of learning and culture: they inform the whole texture of our social and economic structure. The fact that it has become so difficult to accumulate even a comparatively small fortune must have the most profound effects on the organization of business; and it is by no means clear to me that these results are in the social interest. Must not the inevitable consequence of all this be that it will become more and more difficult for innovation to develop save within the ambit of established corporate enterprise, and that more and more of what accumulation takes place will take place within the large concerns which—largely as a result of individual enterprise in the past—managed to get started before the ice age descended? Some of this may be technically inevitable—though a good deal that is said about technical inevitability is ill-founded. But if we are not deliberately working for a time when everything is taken over by the State, is it to be regarded as desirable that it should be so tremendously accelerated by the incidence of a tax system which is the result not of the ineluctable laws of physics, but of very easily modifiable votes of the House of Commons?

Or, to put the question in blunter terms, if our ideal is not universal collectivism but rather property-owning democracy, are we content with a tax system which is working all the time the other way?

V

THE TAX ON MARRIAGE

It is very unlikely that this state of affairs will last for ever. The degree of inequality of net income in this country at the present day is something which, so far as I know, is much less than in any large-scale society at any time in history. Having regard to the great differences in the value of the product of different kinds of effort and enterprise, it seems intrinsically improbable that so great a levelling will be maintained; and this consideration is reinforced when we think of the eventual

political outcome of a system of equality of opportunity in which so high a percentage of the latent talent is given adequate opportunity for all the development of which it is capable—in conditions where all have a chance, the argument against differentiation of reward tends to lose at least some of its force. But all this is looking very far ahead. At the present time, a direct reduction of the progression of the surtax is likely to be a very slow starter.

But this does not mean that all hope must be deferred of any mitigation of the effects of the system. While a substantial reduction of the general progression of the surtax might encounter considerable resistance, a reform of the present system as it affects marriage and the family would probably secure extensive support.

The position under our present tax laws of married persons with independent incomes which add up to more than a certain figure is an anomaly to which attention has frequently been drawn : they would be better off if they lived together without being married. This, of course, is a direct effect of progression ; under a strictly proportionate tax, it would be a matter of indifference whether incomes were aggregated or not. It is a somewhat surprising circumstance, in a community professing respect for the institution of matrimony, that it has been tolerated for so long. For it is in fact a direct tax on marriage—to be more precise, on marriage among the rather better off middle classes.

The Report of the Royal Commission devotes some attention to this problem. But it is perhaps questionable whether its arguments here have the force and cogency which they have in so many other directions.

The Commissioners first point out that this anomaly does not affect all married persons and that it is not until aggregate incomes reach certain levels that the tax on marriage begins. This is true, and, as a corrective of loose statements, is doubtless very much in order. But from the ethical point of view it does not seem to go very far. The tax remains a tax in the instances where it is levied ; and it is surely not a very creditable feature of a tax system that it discriminates between income groups in respect of incentive or disincentive to marriage.

The Commissioners then go on to assure us that it is very doubtful whether the effect of the tax in positively encouraging what they call " more casual associations " is in fact at all extensive. Probably this is true, though, in the ntaure of things,

supporting evidence must have been very hard to obtain. As a people we attach great importance to the married state and we are prepared to make great sacrifices to achieve it. But it is difficult to see how the failure of a policy to produce a certain effect, because of strong resistant moral factors, can be regarded as being in itself a very convincing vindication of the moral status of that policy; we may be gratified that the citizens have not been deflected from virtue by the operation of a certain penalty, but we do not, for that reason, regard the penalty as justifiable. We may be confident that the Commissioners would have condemned in the strongest possible terms a subsidy to "more casual associations." Yet the distinction between immunity from a tax and eligibility for a positive subsidy, though real, is hardly so great as to warrant complete reprobation in the one case and comparative lack of concern in the other. Nor, from the ethical point of view, does it seem that matters are made any better by a warning that the rectification of the anomaly would be expensive to the Exchequer; the greater the expense of rectification, the greater the tax upon marriage.

It is my submission, however, that we should not be content with mere rectification by abolishing aggregation. There is an opportunity here for an innovation of policy which would give marriage and the family a place in the tax system corresponding to our continual lip-service to the national importance of these institutions. Under the American system, roughly speaking, husband and wife may aggregate their incomes and then each be taxed upon a half of the aggregate. Under the so-called "quotient" system prevailing in some other countries this process of aggregation and division is extended to the family, with each child counting as a certain fraction of an adult for purposes of division. A system of this sort solves at one stroke, so to speak, the double problem of eliminating some of the injustice of progression and of providing allowances for children in some measure proportionate to the expenses of the income group into which they are born—a counter-agent to the differential birth rate. The fact that arrangements of this kind are actually in force elsewhere should at least give pause to any tendency to dismiss the suggestion as frivolous. Why should a nation which professes to regard the family as the essential foundation of society not do more to give recognition to that status in its system of public finance? And is there any reason to suppose that change on these lines would be opposed to popular sentiment?

VI
THE DEATH DUTIES

If there is anything at all in the argument of the last section, it would seem to suggest that there is ample scope within the system of the income tax for changes which would foster the decentralized, as opposed to the centralized, influences in our society. The same kind of scope reveals itself if we turn to the field of the death duties.

There can be little doubt that the taxation of property passing at death, as practised at present in this country, is one of the most powerful instruments of change that has ever operated in a great society. This influence is gradual and, save from the point of view of the persons immediately concerned, unsensational. We do not realize from day to day or from year to year what is happening. Yet the relentless working of the estate duty, at its present level of graduation, is such that, within the lifetimes of many now living, the greater part of the great accumulations of the past will have been taken over by the State and the day of the large inheritance will be no more. The great country houses now derelict or used as offices by public boards are an impressive symbol of a process which is ubiquitous.

Now, to use the transition from one generation to another as a means of bringing about social change is, if imposed change be desired, as civilized and as comparatively painless a method as can well be imagined; and it has had the blessing of some of the greatest of our social philosophers. " Would you follow the counsels of equality without contravening those of security ", wrote Bentham, " wait for the natural period which puts an end to hopes and fears—the period of death ". John Stuart Mill thought a progressive income tax an outrage—" a tax on industry and economy " imposing " a penalty on people for having worked harder and saved more than their neighbours "; but he was prepared to do the most drastic things with inheritance. Any law of inheritance is a very artificial thing: there is no *prima facie* case against " interference " in this field.

But it is a profound error to think that all interferences must work the same way. This is demonstrably untrue. A system which enforces a rigid primogeniture will produce a very different kind of society from a system which enforces a mathematically equal division among members of the family.

A partial confiscation of estates passing at death will produce very different results from rules which tend to their division among a number of inheritors.

Now, what is true of the law of inheritance in general is also true of taxation in particular. Different systems will have totally different results. There is all the difference in the world between a system which taxes the estate as a whole on a steep basis of graduation and a system which applies the same graduation, not to the estate as a whole, but to the portions which are received, according to the disposition of the testator, by the legatees. The one system tends to the obliteration of property, the other to its wider diffusion.

The first of these systems, the system which taxes the estate as a whole, is the system under which we now live. And there can be no doubt that if it is desired to bring about a state of affairs in which the degree of inequality due to inequality of inherited property is at a minimum, it works most powerfully in that direction. Although we do not fully realize it, it has already changed the nature of our society most extensively and, if it continues to work at the present rate, it will have changed it altogether before more than two or three generations have elapsed.

But will it have changed it in a desirable way? That is the great question. And, so far as I am concerned, the answer is, quite definitely, no. I have no objection to measures affecting inheritance which tend to remove the more extreme manifestations of inequality. But I have great objection to a system which simply appropriates property, uses the proceeds for current expenditure, and leaves more and more of the functions which used to be discharged by property to be discharged, if they are discharged at all, by the State. The present system is through and through collectivist in its ultimate tendency; and while fully admitting the need for extensive collectivist functions in any well constituted society, I view the prospect in which the collectivist leviathan is confronted only by dependent individuals as a condition which we should seek to avoid.

Contrast the working of this system with the working of a system which differs from it, not necessarily at all in the rate of graduation, but in the unit to which it is applied: the *legacy* rather than the *estate*. Here the tendency is not to obliteration but rather to division. The principle of progression

in this context provides a positive incentive to diffusion. On present rates, a man disposing of an estate of £200,000 would pay nearly twice as much tax if it were bequeathed in a lump as if it were divided in four equal proportions. The effect of such a system, over the years, would be a society almost different in kind, as regards the ownership of property, from the society produced by the working of the estate duty. And from my point of view it would be a much better society, much more robust and independent, much more capable of decentralized initiative, much less liable to mass hysteria and mob movements. It would be a practical realization of some of the ideals, not of a collectivist, but rather of a distributivist society.

Let no one say that such a system is impracticable. For, as we should all know, the rudiments of such a system did actually exist in our own tax system for a very long time. Up to a short time ago, the British death duties included both estate and legacy duty. It is true that, in course of time, the legacy duties had become comparatively unimportant and were probably a great nuisance to the Board of Inland Revenue. But under the chancellorship of Sir Stafford Cripps, the legacy duties were abolished. The estate duty, with its remorseless destructive influence, was left to dominate the scene.

From the point of view of these notes, this was exactly the wrong kind of reform. It was the estate duty which should have been abolished and the principle of the legacy duties made the sole principle of the system. Admittedly, this would have involved a rather more expensive apparatus of administration. But this would have been as dust in the balance beside its beneficial effects in other directions. It is true, too, that it would have involved a loss of revenue. But since the death duties at their present height must be principally paid out of sales in the capital market, any deficit thus created would have had no general disequilibrating influence. The present death duties are a form of tax which can be reduced without serious fear of inflation.

It was doubtless very logical for Sir Stafford Cripps, who was a convinced over-all collectivist, to abolish this form of taxation and to give the estate duty sole sway. It is not plain to me that it is equally logical for the same system to be maintained by those whose Utopia lies in the opposite direction.

VII
PROFIT-SHARING AND SHAREHOLDING

A reform of the death duties on the lines just indicated would be a powerful influence tending towards a property-owning democracy. But it would not be a cure-all. It would only manifest its effects over time. And it would not do anything to change the position of those who at present are propertyless and have no expectations from the propertied.

Now, one of the most urgent problems of the day is somehow or other to give a greater number of people a sense of interest in the nation as a going concern. In a society which is not completely authoritarian there will always be a good deal of sectional bickering about the size of shares in the division of the product; and it is possible to get much too agitated about such inevitable manifestations. But the situation today in which there is the most palpable misapprehension on the part of large sections of the community about the amount that there is available for distribution, still more the conditions under which that amount may be increased, is a genuine cause for concern.

Now it is quite obvious that nationalization is no cure for this frame of mind. Whether or not nationalization brings technical advantages not obtainable in other ways is a matter which is perhaps still open to discussion. But the idea that the workers in nationalized industry have any closer realization of the connection between effort and output and the amount that can be withdrawn from the common pool without involving the enterprise concerned in loss, has been disposed of by the march of events. It may be an exaggeration to say that the workers in a nationalized industry have less sense of responsibility than workers elsewhere. But it would certainly be quite absurd to say that they have more.

To meet this situation the claims of profit-sharing are often canvassed. If the workers in an industrial establishment are given a direct share of profits, it is urged, they will come to have a sense of solidarity with its interests and some understanding of its problems. The solution of the class struggle is the extension of this kind of arrangement.

I would not question that there is a good deal to be said for this position. A great volume of experience seems to suggest that in establishments where genuine profit-sharing schemes have been introduced and where it has been possible to persuade the wage-earners that this was no mere device for upsetting the

normal process of wage-fixing, relations between management and workers have very greatly improved. It has even been suggested that in a certain constituency at the recent general election a substantial number of wage-earners were moved to change their political allegiance on the ground that the nationalization with which their firm was threatened would upset the arrangements for profit-sharing.

Nevertheless, profit-sharing is not a radical solution. An entitlement to a share in profits on this basis is not property. It cannot be bought and sold. It does not carry with it a liability to loss. It involves no proportionate voice in control. There is an essentially *ex gratia* element in it all. A profit-sharing democracy is not necessarily a property-owning democracy.

I do not think it is at all desirable to attempt to remedy these deficiencies by introducing an element of compulsion. The idea of compulsory profit-sharing creates more problems than it solves. It rides roughshod over the rights of existing shareholders. Its incidence and its benefits are unequal as between companies with different degrees of financial gearing. There is no common rate of sharing which is appropriate to all types of industry. It involves privilege without responsibility and confers none of the reserve power of real property. I should regard the introduction of compulsory profit-sharing as likely to do much more harm than good.

If we ask ourselves what is the ideal solution to this problem from the non-collectivist point of view, the answer is obvious: the workers should themselves own equities. The solution to the lack of responsibility and solidarity which comes from an insufficient diffusion of property is a greater diffusion of property. There is nothing wrong in the property system itself. The result of the evolution of many ages, it solves a great many economic and social problems which otherwise would be insoluble. The trouble is that it is not yet sufficiently widespread. It is not necessary that everyone should be a property owner or that all ownings of property should be equal. But it is highly desirable that more people should own property.

If this is so, it has a very immediate bearing on the problem under discussion. If the owners of industrial undertakings feel moved to take deliberate steps to bring their workers into more intimate association with the prospects of their company and with the prosperity of industry in general, the best thing for them to do is to make their distribution in the form of shares.

They should seek on a large scale to make equity owners of the workers. An unconditional share in the equity, rather than a conditional share in the profits, is the appropriate solution to many social and industrial problems.

Now—and this brings us back to the main contention of these notes—this is a development which can be either greatly impeded or greatly facilitated by tax policy. Hitherto, I do not think it can be denied that the tax laws have been so many obstacles to be circumnavigated. Imaginative schemes on these lines have had to be shelved because the liability to tax, in some form or other, made the scheme either inoperative or unattractive. But there is nothing in the nature of things why this should continue to be so. It is easy to think of a number of ways in which the bias should work in the opposite direction and, so far from deterring distributions on these lines, the tax system positively favour them.

It is, of course, very easy to think of objections. Certainly, any attempt to change the law in this way would have a rough passage at the hands of the defenders of the logic of the existing tradition. Why should companies fortunate enough to be in a position to carry out such schemes receive the added benefit which would be provided by deliberate stimulus through tax reductions ? Why should workers who receive such distributions be exempt from the obligation to regard them as income ? And so on and so forth. To all of which the answer is that the gain from inconsistency in this respect is judged to be vastly more significant than its disadvantages. For this is not a mere matter of a-year-to-year assessment of tax liability : it is a matter of deliberately producing an important shift in the property structure and an important gain in social and economic solidarity. As we have seen already, there is nothing particularly neutral in the operation of the present tax structure. Relentlessly, year by year, it is pushing us towards collectivism and propertyless uniformity. Why then should we not begin to use it to produce change in another direction ?

LIONEL ROBBINS.

The London School of Economics.
25th August, 1955.

The Case for Investment and Productivity

By Professor Ely Devons.

SINCE the end of the war there has been a continuous flow of speeches and articles from economists, journalists and politicians telling the public how important it is to increase productivity in British industry and to have a high rate of investment in order to achieve this. If we do this, we are told, the economic prospect before us is bright and promising, full of hope for a continuously rising standard of living; but if we don't, we shall be in a perpetual state of economic crisis, ever on the verge of economic bankruptcy.

Very often when the need for productivity increases and investment is explained, the arguments used imply that there is a critical rate of increase; that if we achieve this rate all will be well, but if we fall below it we shall be in recurrent difficulty. This view is frequently expressed in the literature which the British Productivity Council puts out to British industry. " The British standard of living cannot be maintained, let alone improved ", the Productivity Council states in an outline of its objectives, " unless our productive efficiency keeps pace with that of other countries ". Yet " we are convinced that Britain can, nevertheless, in due course enjoy a standard of living second to none ". This seems to imply that if we do what is necessary in taking measures to improve productivity we shall have a standard of living rising by 3 or 4 per cent. per annum but that if we do not we shall have great difficulty in preventing our standard from falling. Intermediate positions, with a slow but still marked rate of improvement, are not envisaged. It is as if we are forced to choose between penury and prosperity, between a rapidly rising standard and a stationary or falling one.

This view, which implies a certain discontinuity in possible rates of economic progress, has a great appeal. For it enables the economic problem to be posed to the public in clear black and white. Either we do what the economists and politicians say is necessary and then all will be well; or we neglect their advice and face disaster. Either, by increasing productivity and investment, we raise the standard of living by a substantial rate year by year, or we have no increase at all. Against such a background, it is easy to see how particular rates of progress and investment become accepted as the right ones to go for. In this country the fashionable objectives are a 3 per cent. rate

of increase in the standard of living, and 20 per cent. of the national income devoted to investment.

In this article I try to examine the basis of these views and particularly to see what economic arguments, if any, there are for picking out a particular rate of increase in productivity, or figure of the ratio of investment to national income, as targets of economic policy, whether there is from the economic point of view an "ideal" rate of progress or a range of rates, each with its own problems, costs, consequences and advantages. It may be, of course, that although there are no compelling economic arguments pointing to the conclusion that there is only one rate at which we can go forward, yet there may be powerful political reasons why we should prefer a high rather than a low rate of increase in productivity and output.

II

I ignore at this stage the way in which our dependence on foreign trade affects the argument, not because this is unimportant, but merely in the hope that the issues involved will be clearer if we deal with this separately later. If we confine our attention to our internal economic situation then the argument for increasing productivity is largely tautological. Production and consumption are merely two sides of the same coin. Rising real expenditure per head can only come from rising production per head; if production per head increases year by year by 1, 2 or 3 per cent., then expenditure per head can also rise by 1, 2 or 3 per cent. In the short run it may be possible to increase consumption at the expense of investment or other uses of economic resources; but over the long period the rate of growth of the standard of living, if this is measured in the goods and services per head of the population, cannot diverge from the rate of growth in production per head, or productivity. Of course, if one measures productivity in terms of production per head of the working population alone, or in terms of production per man-hour, then there may be some divergence between the movements of productivity and national income per head, because of changes in the ratio of the working population to the total, or in the average number of hours worked.

Clearly a rise in productivity of 3 per cent. per annum gives a more rapidly rising standard than a rise of 1 or 2 per cent. per annum, but there is here no compelling economic basis for arguing that 3 per cent. is the right figure to go for. It may be a striking way of explaining to the public what an annual increase of 3 per cent. in the rate of productivity means,

to say with the Chancellor of the Exchequer that this would enable us to double the standard of living in the next 25 years. But this is a lesson in arithmetic, not in economics. And the laws of compound rates of interest could be illustrated just as well by taking some other rate: to say, for example, that a $2\frac{1}{2}$ per cent. rate of increase would mean a doubling of the standard of living in 30 years.

If one looks at the relationship between productivity and the standard of living in this simple way, then for any rate of increase in productivity we care to assume there is a corresponding rate of increase in the standard of living. There is so far no basis for arguing that it is either all or nothing, or that a particular rate of increase is the right one.

This is not to deny the importance of getting people to realize that, in the long run, increases in the standard of living can come only from increased production, that they cannot be obtained through the magic of government manipulation of taxation or subsidies, and that this applies just as much to the volume of public services—health, education, housing and defence—as to private consumption. And if the politicians make up their minds that the public will be discontented if they do not have rising wages, a rising standard of living and increased welfare services, then there is no doubt considerable political justification for them to urge on the public the need to increase productivity. Whether there are grounds for believing that it is 3 per cent. per annum that will keep the public happy is quite a different matter.

It can be argued that it is largely ignorance which impedes a high rate of increase in productivity, that if managers and workers alike could be made aware more quickly of improved and more up to date methods of production, progress would be much more rapid. But where increasing productivity involves such changes in organization, traditional habits and customary methods of work as to create social disturbance and the breakdown of old patterns of living, the position is not so clear. Who is to say that the cost is worth paying? There is certainly plenty of room for difference of opinion here, as one can see, for example, by reading the speeches in the recent debate in the House of Commons on the report of the Monopolies Commission. The economist is inclined to argue that the temporary disruption is worth while if in the long run it leads to increases in productivity and the standard of living. The whole tradition of economic thinking sets a high value on material progress. One can argue at great length about the cost and advantages of more or less rapid rates of economic progress without getting

very far. For even if we know with reasonable reliability what the costs and advantages are, there is no agreed basis for weighing one against the other. Certainly, there is no economic argument which points to the conclusion that with a 3 per cent. rate of increase the benefits balance the costs and that at any lower rate the benefits clearly predominate.

III

The case for a high rate of investment is mainly based on the need to invest in order to raise productivity and the standard of living. Of course, if we pick on a particular long-run rate of increase in the standard of living as the desirable one, it is in theory possible to say that we must devote some particular proportion of our resources to investment, otherwise the increase will not be achieved. In practice, even so, we cannot say with any reliability in quantitative terms what the necessary relation is between investment and particular rates of increase in productivity and production. We can get little further than to say that increased investment will make for a more rapid rate of increase in output. We benefit from the investment of the past, and the more we invest now the greater the material benefits we provide for ourselves and generations in the future.

A diversion of more resources to investment involves less consumption or public services now. By what criteria do we decide, as a nation, how much jam we should give up today in exchange for the promise of more jam tomorrow? Suppose we knew, for example, that devoting 20 per cent. of the national resources to investment (and leaving 80 per cent. for consumption and public services) would yield a 3 per cent. rate of increase in productivity in the long run, whereas to devote only 15 per cent. to investment (leaving 85 per cent. for the other uses) would yield only a 2 per cent. increase. How do we choose between the two? When investment depended mainly on the savings of the rich there seemed to be a strong case for urging them to save and invest rather than to engage in profligate personal expenditure, since such investment would benefit the mass of the population in the long run. But now a high rate of saving and investment means a restriction of consumption for a much wider section of the population, and the argument is not so obvious.

No doubt some people would contend that the " natural " rate of interest, balancing the demand for and supply of savings, would secure the " right " rate of investment for the country as a whole. The relation between the actual rate of interest and such a " natural " rate and the effect of the rate of interest on

investment, are matters which raise controversial issues outside the scope of this article. In any case such an argument is not really relevant to the point I am trying to make. For it still leaves open the question whether we should take special action to increase the supply of savings by education, propaganda and budgetary policy and to increase the willingness to invest by special taxation and other provisions favouring investment and by manipulating the rate of interest through monetary policy.

Frequently it is contended that we need a high rate of saving and investment in order to take advantage of the promising technical innovations that rapidly advancing science produces in ever increasing flow; and that the provision to a wider and wider public of new and ever changing consumer goods—cars, refrigerators, washing machines, television sets, and so on—demands more and more capital equipment. In part, this is no more than a special case of the more general argument that we must have a high rate of investment in order to have a high rate of increase in standards of living in the future. In so far as technical innovation by itself is going to lead to increased productivity and higher living standards anyway, it can be taken as an argument both for and against higher investment. For when technical innovation is rapid the opportunities for investment are greater and the returns from investment are higher; and this makes investment more attractive. But our reaction to such rosy prospects for the future may be a willingness to forgo less, rather than more, from our present standards. If our children are going to have the benefits of atomic power, automatic factories, and other yet unheard of industrial miracles, why should we strain ourselves now in order to add yet further to their standards? If we are really on the verge of a new industrial revolution with great potentialities for increasing productivity, is it really vital to push up investment now? Cannot we take advantage of the great new opportunities a little more slowly?

Some people would argue that an intermediate rate of innovation is not really possible. On the one hand, you may have a business community that is energetic, adventurous, anxious to take risks, seizing every opportunity for increasing efficiency; such a business community will not be satisfied with a slow rate of innovation. And a society which produces such a business community is likely to be one which puts a high value on material progress and, therefore, one in which workers are also willing—indeed anxious—to accept new techniques and methods of production which give them a higher standard of living. On the other hand, the business

community and workers alike may be bound by tradition and customary ways of doing things, unwilling to consider new methods and ideas, and taking little interest in new techniques and new products. Between the two, it may be argued, there are no stable intermediate stages: a society may have periods of rapid innovation and economic development or periods of stagnation, but slow gradual increase is rare. This is a view which one cannot easily substantiate or refute. At first sight, it is hardly supported by the experience of the United Kingdom in the last 50 years, where there has been a sluggish but still quite definite rate of increase in productivity and a continuous if not spectacular rate of innovation.

The case for high investment is often supported by pointing to the poor state of existing capital in this country: for example, the railways and the roads. And perhaps it is true that in relation to other items of capital expenditure, such as housing, too little has been spent on these in the post-war period. But this raises the issue of the right distribution of investment, rather than its general level.

There is also the argument that a high rate of investment is necessary to keep the economy fully employed; that without it resources would be idle and labour unemployed. In such circumstances investment is all benefit; there is no question of weighing up jam today against more jam tomorrow: we have both. This was a fashionable and perhaps relevant argument in the 1930's and it still apparently plays some rôle in economic discussion in the United States; but it has little bearing on the economic situation in this country since the war.

IV

If we have regard to our internal economic situation only, therefore, there seem to be no clear compelling economic reasons why we should pursue a high rate of increase in productivity and devote a substantial proportion of our resources to investment. Our policy and actions, both individually and collectively, could be related simply to the value that we place on a rising standard of living, and how far we are prepared to forgo benefits now in order to enjoy higher standards later. How does our dependence on foreign trade complicate and alter the position? It is, of course, usually argued that whatever choice we might have otherwise, the need to compete overseas compels us to take measures to increase our efficiency and productivity and to undertake the investment which is necessary for this. Otherwise we shall be in continuous difficulty in competing in export markets, will be unable to buy the food

and raw materials that we want, and will be in chronic balance of payments difficulty.

Our competitive position overseas depends to a substantial degree on the prices that we demand compared with other suppliers. Prices are a function of raw material prices, wage rates and other costs, as well as of changes in productivity. Over imported raw materials costs we have little control, but we can hope that in the long run we do not have to pay any higher prices than our main competitors. For the other factors, the higher the level of productivity in relation to money rates, the lower the level of prices. It is the combination of the two that is crucial. In the case of labour, for example, the combination of the movement in money wage rates or money earnings and labour productivity. What matters is the effect of the two together on prices in relation to those of our competitors. If productivity in export industries here and in the U.S.A. is increasing by, say, 4 per cent. per annum, while wage rates here are increasing by 6 per cent. and in the U.S.A. by 4 per cent., inevitably our prices will become less competitive.

The competitiveness of our exports depends, therefore, not only on the rate of increase in productivity here, but also on the rate of change in wage, salary and other money income compared with that occurring overseas. Our monetary policy has to be geared closely to events overseas. If our main competitors, U.S.A. and Germany, are going through an inflationary phase, with incomes and prices rising substantially, we can afford, if we wish, to allow the same to happen here. But if they are keeping their prices, especially their export prices, stable, whereas we allow our money incomes, especially in export industries, to rise more than the increase in productivity, we are courting trouble. Relative movements in productivity are clearly an important element in the situation, though not necessarily the most important. We cannot escape for long from keeping our monetary policy in line with that of other countries by pressing for greater increases in productivity. No doubt, if money incomes here are increasing by 3 per cent., the problem of maintaining our position in export markets is easier if productivity is increasing by 3 per cent. rather than by 2 per cent. or not at all. But there is no magic in the rate of 3 per cent.; there is no guarantee that at this rate money incomes will rise no more than productivity, and that our export prices will be at the right level compared with those of other countries.

It can indeed be argued that the very circumstances which are conducive to a high rate of increase in productivity are themselves likely to lead to money incomes rising even faster

and to our prices becoming too high—unless, of course, the same forces are also in operation in the economies of our competitors. Suppose it were true that workers will agree to the introduction of new techniques and new labour saving methods of production, which are a necessary condition of a high rate of increase in productivity, only if there is so high a level of employment as to produce an acute shortage of labour. Suppose also that businessmen will not invest at a high rate and explore new ways of increasing output and efficiency unless they see a guaranteed and expanding market for their output. Suppose, in other words, that conditions of inflation or near inflation are necessary to get a high rate of increase in productivity. It is because they take this view that many people regard mild inflation with favour. But these are the very conditions which make it easy for everyone to demand increases in money incomes beyond the increases taking place in productivity, and which give an upward twist to our export prices. They are also the circumstances in which demand in the home market is so great that exporting, usually more troublesome and risky, is neglected. So that although a high rate of increase in productivity may appear to help to keep us competitive overseas, if such an increase can only be secured at the cost of continuous inflation, the advantage overseas may, in the short run at least, be more than offset by the other consequences of such inflation.

Pressure for a high rate of home investment may have similar consequences. In the long run it may mean increased efficiency and competitiveness overseas. But in the short run pressure for increased investment at home, especially if it is accompanied by an easy budget policy, itself adds fuel to the inflationary forces. And many of the goods needed in industrial investment, especially engineering products, are among those which are easiest to sell abroad. It is hardly surprising, therefore, that at times of incipient balance of payments trouble, the official pressure urging more investment is relaxed; indeed, that there is often even an attempt to go into reverse. Rarely at such times does one hear the argument that we should invest more, in order to increase productivity still further and so make exports more competitive.

It is the whole set of forces which influence the incentive to export and our export prices in relation to those of our competitors that need to be watched. To pick out productivity or investment and concentrate attention on these at the expense of everything else will merely mislead us. If a near-inflationary situation at home, with negligible unemployment, is a condition

of a high rate of increase in productivity, then this will aggravate rather than alleviate our overseas position, at least in the short run.

International comparisons of movements in money costs, prices and productivity are extremely difficult to make. The following table shows the movement in money wage rates and export prices of manufactures for the United States, Germany and the United Kingdom since 1950. The figures have to be used with great caution. There are no indices of wage rates for the United States and Germany, and the figures of hourly earnings are affected by the changing amount of work at overtime rates, variations in piece rates, as well as shifts in employment. The composition of trade in manufactures is different for the three countries and this affects the movement in the indices of average values.

Wages and Export Prices in U.K., U.S.A., and Germany

1950 = 100

	United Kingdom			United States		Germany	
	Weekly Wage Rates	† Av. Hourly Earnings in Manfctg.	Export Av. Value of Manfcts.	Av. Hourly Earnings in Manfctg.	Export Av. Value of Finished Manfcts.	Av. Hourly Earnings in Manfctg. and Building	Export Av. Value of Finished Products
1951	108	108	117	109	111	115	115
1952	117	119	125	114	112	124	126
1953	123	125	122	121	112	129	125
1954	128	132	119	124	113	132	121
1955	137*	143	121*	128 ‡	112 ‡	137 §	122 §

* June † April each year ‡ May § First quarter

In the period of the Korean boom, which was still to some extent a period of adjustment to the effects of devaluation in the United Kingdom, wage rates and export prices rose more in Germany and the United Kingdom than in the United States. During this period the United Kingdom used up a substantial part of the price advantage over the United States that was obtained by the 1949 devaluation of sterling. From 1952 to 1954, however, export prices were steady in all three countries. The remarkable stability in prices of United Kingdom manufactures is confirmed by the Board of Trade new index of the wholesale price of manufactured products. This rose steeply from 103 (June, 1949 = 100) in January, 1950, to 129·6 in March, 1952, and then remained stable until the end of 1954 (126·3).

Wage rates in the United Kingdom have taken a leap forward since the beginning of 1955, and by June were already

$5\frac{1}{2}$ per cent. higher than at the end of 1954. There is no evidence that current increases in productivity are sufficient to absorb such wage increases without affecting prices. The index number of prices of exports of manufactures has increased by 2 per cent. in the first six months of this year, the main increase being in the index for metals; and the wholesale price index of manufactured products began to move up appreciably from the beginning of the year (by 2 per cent. to June). But it is not easy to tell how far this is a reflection of wage increases and how far the delayed effect of imported raw material prices, some of which—for example, those of non-ferrous metals—have risen markedly since the beginning of 1954. The effects of these movements on the competitiveness of British prices depends a good deal on whether there is similar wage pressure in the United States and Germany. So far this year the increases in those two countries seem to have been on a smaller scale than in this country.

V

The last section was mainly concerned with the effects in the short run of pressure to increase productivity and have a high rate of investment on our competitive position abroad and the stability of the balance of payments. If we attempt a longer run view, the conclusion we come to depends on the assumptions we make about the various forces at work; and we can have as many different conclusions as combinations of assumptions we care to take.

Only a combination of all the most gloomy and pessimistic assumptions would lead to the conclusion that in the long run "the British standard of living cannot be maintained, let alone improved, unless our productive efficiency keeps pace with that of other nations." Such a statement implies that our competitors use rising efficiency in their export industries mainly to reduce their prices, and take little of the benefit in rising money incomes to those engaged in these industries; as a consequence, to maintain our exports, we should have to reduce our prices too. If our productivity is not rising as much as that of our competitors, we could do this only by reducing money incomes or by progressive devaluation. If we assume that at the same time there is little or no increase in productivity in food and raw materials production, and that the relation between world demand and supply results in ever increasing difficulty in our getting imports, then we should also be faced with the prospect of having to pay higher and higher prices for our imports. Such an adverse movement in the terms of trade could

theoretically be sufficiently large to offset completely rising productivity here, so that we should need substantial increases in productivity merely to prevent our standard of living from falling. We should have to run faster and faster merely to stay in the same place.

I cannot see that there is evidence for taking such an extremely gloomy view of the future. If there were, all talk of doubling our standard of living in 25 years would be miserable deception; for the unfavourable forces implied in these assumptions do not disappear if we have increasing productivity at 3 per cent. per annum rather than 1 or 2 per cent. per annum, or if we devote 20 per cent. of the national income to investment rather than 15 per cent.

The long-run problem of competing overseas may reinforce the need for high investment, especially in export industries, from a different point of view. Over the years, competitiveness in price, which we might be able to secure by restraining the rise in money incomes here or by manipulating the exchange rate, may not be enough. If our competitors, through technical advance and innovation, are offering new products, we are not likely to be able to sell goods which are out of date, even if these are relatively cheaper. In many markets, especially for machinery and equipment, it is superiority in operation and design, rather than difference in price, which affects the volume of sales. And we can only hope to be able to offer the most up to date products, the argument runs, if we have a rapid rate of technical and product innovation at home, which in turn is not possible without substantial investment in manufacturing industry. This is a powerful argument for keeping innovation here abreast of that of our main competitors. But it is as well to keep in mind that in fact the needs of investment in the export industries are only a small part of total investment, and that even here it is hardly a question of all or nothing.

If we have a high rate of increase in productivity and investment, will it help the balance of payments in the long run? Here again the answer depends on the assumptions one makes. At first glance it is difficult to imagine that it could do other than help. But there are some who would argue that given our heavy dependence on imports for food and raw materials, rising production and incomes in this country may make our underlying balance of payments progressively more difficult. As our production increases, it is argued, we shall have to import more raw materials and as our incomes increase we shall want to import more food. If at the same time world trade in manufactures is not growing at a sufficiently rapid rate, we

may find chronic difficulty in expanding the volume of our exports. On this view, the more successful we are in the long run in raising production at home, the higher the level of foreign trade, both imports and exports, which will be required and the more difficult it will be to secure this. As with many other arguments in this field, it is difficult to produce the evidence either to substantiate or refute this view. But the fact that it should be held at all at least serves to illustrate the point that there are no obviously compelling balance of payments arguments which point to the need for rapidly increasing production and productivity.

VI

The economic arguments for a high rate of investment and rate of increase in productivity prove thus to be neither simple nor obvious. And it is hardly surprising, therefore, that those who support the case for productivity frequently fall back on political arguments. The line of reasoning is very familiar. For reasons of international prestige and in order to maintain our standing in the world we must keep abreast of the other leading nations in the economic race. Other countries, especially the backward areas of the world, will be much more impressed by the British way of doing things if they see that we have a standard of living rising as rapidly as that of any other country. Rising productivity here will make it easier for us to contribute to the economic development of such backward areas, and this is desirable on humanitarian as well as political grounds. With higher production per head we shall no longer need to rely on the United States for contributions to our defence, and so will avoid the embarrassment of appearing to be committed by such aid to supporting United States policy. With greater wealth we will in any case be able to spend more on defence should this be necessary, and if we make a greater contribution to the defence of the West we can expect more notice to be taken of our views in international political negotiations. Such arguments, and many others on similar lines, seem to provide a more powerful and straightforward basis for urging the need for increased productivity and a high rate of investment than any economic argument. For in essence the economic argument amounts to little more than saying that if we want a rising standard of living we must do what is necessary to achieve a rising volume of output.

Ely Devons.

University of Manchester.
August, 1955.

Automobiles : The Mass Market

By George Wansbrough

IF our standard of living is to double in the next 25 years, the increase in the national income will be achieved above all by the fullest possible development of the most promising of our industries. Some aspects of the claims of the automobile manufacturing industry to be included in a very short list of our most promising industries are here examined, and deductions made as to the conditions necessary to secure that it makes the greatest possible contribution to national prosperity.

The automobile manufacturing industry proper can be divided, like Gaul, into three parts. There are the Big Five manufacturers : the British Motor Corporation (Austin, Morris, etc.), Ford, Vauxhall, Rootes and Standard, who between them make all but about a tenth both of the passenger cars and of the agricultural tractors made in this country, and a slightly smaller proportion of the commercial vehicles. There are the smaller passenger car manufacturers : Jaguar, Rover, Daimler (part of B.S.A.), Armstrong Siddeley (part of Hawker Siddeley), Rolls Royce and others, with outputs ranging from 200 to 250 a week downwards. There are the builders of heavy commercial vehicles, mostly of five tons and over, from the Leyland-Albion group with an output of perhaps 300–400 vehicles a week (not to mention quite a number of tanks), through a surprisingly long list of firms making road transport equipment which fulfils an economic demand.

Supplying the automobile manufacturers proper are a host, whom no man can number, of other manufacturers, ranging from such giants as Dunlop (whose turnover exceeds that of any vehicle manufacturer), Joseph Lucas and Smith's Instruments down to minuscule firms making, often for several of the big factories, some component part more economically than the latter can make it themselves. Purchased components and raw materials form a large part of the total cost of a motor car. Even in the case of General Motors Corporation, with enormous ramifications backwards into quasi-independent factories making such things as ball bearings, radiators and electrical equipment, purchases amount to just one half of the Corporation's sales. For the chief British factories, the proportion is 55–70 per cent.

In this article the discussion is confined to the producers of cars for the mass market. No reference is made to the specialist producers either of heavy commercial vehicles or of

the more expensive cars, both of which make a considerable contribution to exports and also to the engineering prestige of the country. The argument is based, so far as it relates to manufacturing costs, on the figures of the Big Five manufacturers, who make practically all this country's output of motor cars retailing for less than £1,000, of agricultural tractors, and of commercial vehicles of less than six tons capacity. The picture would be more complete if figures of the component manufacturers were added, since their net contribution to the final product is not much smaller than that of the vehicle manufacturers themselves; but their manufacturing techniques are for the most part similar, and their costs can be expected to show a similar relation to output.

I. INCREASING MANUFACTURING ECONOMY

Last year the total production of cars and commercial vehicles by the British automobile industry for the first time exceeded a million vehicles. For the first four months of 1955, a further increase of better than 25 per cent. has been achieved. Leading manufacturers have announced various major plans for expansion over the next few years, which are likely to lead to increased output and lower manufacturing costs. It is an opportune moment to examine the performance of the last few years to see how the expansion which has already occurred has led to lower relative costs, and to consider the likely effect of further expansion.

Since the picture is an encouraging one, it is as well, in order to avoid exaggerating the rate of progress, to select as a base year one which was a good year for the industry, namely 1950. In that year there was a temporary peak in the volume of output, as the following figures show:

Output of the U.K. Automobile Industry

	Cars	Commercial Vehicles	Agricultural Tractors	Total
1948 ..	334,815	177,261	114,341	626,417
1949 ..	412,290	218,375	88,209	718,874
1950 ..	522,515	262,702	117,445	902,662
1951 ..	475,919	259,193	137,387	872,499
1952 ..	448,000	242,372	122,808	813,180
1953 ..	594,808	240,093	109,327	944,228
1954 ..	769,165	270,025	133,048	1,172,238

The 1954 output was 30 per cent. in excess of that for 1950. The first test of improved productivity is the comparison

of the value for money offered, offset by the increase in the level of costs of labour and material to the manufacturers. Taking labour first, the average earnings of those engaged in the manufacture of motor vehicles and bicycles for April, 1954, was £11 5s. 2d. per week, against an average of £8 8s. 5d. per week in April, 1950, an increase of 33·7 per cent. The earnings of those in the industries supplying the motor car industry with its components and sub-assemblies showed a sufficiently similar increase to justify our taking a figure of one-third for the increase in labour costs per man-hour. The index number of wholesale prices of materials used in the mechanical engineering industry (mid-1949 = 100) rose similarly, from 113·2 to 150·4 or by almost exactly one-third. Thus the costs of man-hours and of materials used by the industry in 1954 were one-third higher in 1950.

To give a fair comparison of the selling prices, it is necessary to allow for the additions and improvements made to the various models, so far as these have led to increases in weight; for, other things being equal, these changes would increase manufacturing costs by amounts approximately proportional to the increase in weight. Thus the comparison is best made on a basis of weight in pence per lb.

There were important differences in all the principal models in substantial production in 1950 and in 1954 respectively by Austin, Ford and Vauxhall. Nevertheless, making a comparison on the basis of pence per lb., it is just to compare in the case of Austin, the A.40 of 1950 and the A.40 of 1954, and in the case of Vauxhall the Velox of 1950 and the Velox of 1954. In both cases the improvement from the *customer's* point of view of the 1954 model is not exaggerated by the increase in weight (5½ per cent. and 7 per cent. respectively), while the extra manufacturing cost of the later model could be expected, other things being equal, to be fully proportionate to the increase in weight. The Ford Anglia of 1950 and the Ford Popular of 1954, on the other hand, are different cars, largely aimed at different markets; nevertheless, there is so much in common between them that it seems fairer to include them in the comparison rather than to leave this very important manufacturer out of the comparison.

A simple average of the increases in pence per lb. shown in the table overleaf is less than 10 per cent. Improvements have been embodied, at some cost, in every one of the cars listed: overhead valves engines in the Morris Minor and the Hillman Minx in place of side valves; an engine of 1,172 c.c.

capacity in the Ford Popular against the 933 c.c. engine of the 1950 Anglia; more luggage accommodation in the Standard Vanguard; a more powerful engine and a much roomier body in the 1954 Vauxhall Velox compared with the 1950 Velox, and so on. Having regard to these improvements, it is certainly not understating the increase in prices to say that, in spite of the decline in the value of money, £110 in 1954 would buy as much motor car as £100 in 1950. Against an increase in costs of one-third, it may therefore roughly be said that the industry in 1954 was bettering its 1950 performance in the real value offered to its customers by as much as 20 per cent. This was accomplished during a period in which the volume of output of cars increased by 47½ per cent., of commercial vehicles by 3 per cent., and of tractors by 13 per cent.[1]

It is clear from the figures that the improvement has not been achieved by any massive re-equipment. The total of fixed assets employed increased, at net book values, by 57 per cent., from £39·8 millions to £62·6 millions. Gross book values (i.e. before depreciation) of land, buildings, etc., increased by £7·7 millions, or 37 per cent., and of plant and machinery by £37·2 millions, or 70 per cent. While the total gross capital expenditure of between £45 and £50 millions is a formidable amount, it is a long way short of the amounts likely to be spent in the next four years. Allowing for the fact that a considerable part of the fixed capital of the industry in 1950 consisted of assets, particularly buildings, acquired at lower price levels, it seems likely that the fixed assets employed,

Saloon Model	Dry Weight (Partly Estimated) cwt.		Retail Price (Excl. P.T.)		Do. in Pence per lb.		Increase 1954 over 1950
	1950	1954	1950	1954	1950	1954	%
Austin A.40 ..	19·0	20·1	£392	£468	44·3	49·8	12·4
Ford Anglia ..	14·5		£257		38·0		
Ford Popular ..		14·5		£275		40·6	6·8
Hillman Minx ..	17·8	18·75	£395	£458	47·6	52·4	10·1
Humber Hawk ..	24·6	26·6	£625	£695	54·4	56·0	2·9
Morris Minor ..	14·75	15·5	£299	£373	43·4	51·6	18·7
Standard Vanguard ..	23·5	24·1	£515	£555	48·0	49·4	2·9
Vauxhall Velox ..	20·3	21·8	£430	£535	45·4	52·5	15·7

[1] It is not practicable to calculate a figure for the increase in total physical output, especially since, with a growing volume of vehicles in circulation, there must have been a substantial increase in the production of spare parts. This is illustrated by the increase of exports of parts and accessories (excluding tyres) by 84 per cent., from £36·4 millions in 1950 to £67·1 millions in 1954.

if valued at a constant price level, would not have shown a proportionate increase from 1950 to 1954 much greater than the increase in the physical volume of output and perhaps even less than proportionate.

More light is thrown on the problem by considering the development of the separate manufacturing groups, since some of them give more detailed information than others, and also because they are at different phases in their expansion programme.

Both Ford and Vauxhall seem now to be at the end of one phase of their development and to be embarking on a fresh pattern of expansion. Vauxhall's operations have, until recently, been closely concentrated at Luton. The number of units produced in 1954 showed an increase of almost 50 per cent. over the output for 1950. The percentage increase in the number of passenger cars was greater than that in the number of commercial vehicles,[1] whose value per unit is higher. On the other hand, since 1950 Vauxhall's have extended their production of commercial vehicles to a greater degree into the larger size of trucks. Allowing for the increase in the size of their passenger cars, and for the increasing proportion of spare parts business, an increase of more than 50 per cent. in the physical volume of output is consistent with the figures. The total money turnover in 1954 showed an increase of 110 per cent. over 1950, which even on the assumption that prices rose by as much as 25 per cent. would still indicate an increase in physical output of 68 per cent. over 1950. By comparison, there was an increase of only 25 per cent. in the labour force, of 30 per cent. in the gross book value of land and buildings and of 67 per cent. in the gross book value of plant, machinery, equipment and tools.

In physical terms, therefore, and eliminating the effect of price changes, it seems as though an increase of some 60 per cent. in volume of output was achieved with an increase of less than that in the physical amount of capital employed and of only 25 per cent. in the amount of labour employed. That is to say, the amount of capital employed per unit of output was no greater, while the average amount of direct labour per unit was reduced by some 22 per cent.

The increase in productivity must therefore be attributed not so much to the installation of labour saving machinery,

[1] Commercial vehicles have for many years been a much greater proportion of Vauxhall's output than the other four manufacturers.

important though the part this played must have been, as to the more intensive use of physical resources, more efficient flow of materials and so on: in short, to an all-round increase in manufacturing efficiency and economy, due, above all, to an increase in volume.

In the latter part of last year it was announced that Vauxhall's were embarking on a programme of expansion estimated to cost £36 millions, or almost twice the gross amount of fixed assets employed at the end of 1954. The object is to double the 1954 output. Part of the new facilities is to be at Dunstable, and it is apparent that much of the capacity to be created must be elsewhere than at Luton. The programme of expansion is believed to include an extension of the range of Vauxhall cars into the small car market, in which Vauxhall has never before been represented.

It is doubtless inevitable that at first new productive capacity, away from the existing centre, will be less efficient than the older established plant operated, as it were, at saturation point. Any such effect is likely to be short-lived and to be swamped in the over-all cost figures by the continuing expansion of output. On the basis of past experience, it would probably not be over-optimistic to guess that when the whole expansion is completed and the facilities are used as close to saturation point as the existing facilities were in 1954, there will be a reduction of costs, on a pence per lb. of product basis at constant prices, of as much as 20 per cent.

The position of the Ford Motor Company is in many ways parallel to that of Vauxhall's. Their production was concentrated at Dagenham to as high a degree as Vauxhall's at Luton, and the manufacture of their bodies by Briggs was in close proximity. The acquisition of Briggs by Ford early in 1953 brought under Ford control factories at Eastleigh and at Doncaster; and it is clear that Ford's new programme of expansion estimated to cost £65 millions is likely to involve the development of substantial manufacturing capacity away from Dagenham.

The increase in money turnover (adjusted to include for 1950 Briggs' sales other than to Ford) was 80 per cent. The increase in the number of vehicles produced was 57 per cent. and allowing for the increase in spare parts business it seems likely that Ford's effective output in 1954 was some 60 per cent. greater than in 1950. The increase in the number of employees (including Briggs for both years) was about 40 per cent., while the increase in gross book value of fixed assets

employed was 60 per cent., though this again, as with Vauxhall's, must overstate the increase that a valuation at constant prices would show.

The proportionate increase in fixed assets which will be the result of the £65 millions expansion programme, compared to the gross book value at the end of 1954 of £42½ millions, is not so great as Vauxhall's. No figures have been announced of the increase in productive capacity which is aimed at, but the reduction in manufacturing costs which the expansion programme is likely to achieve may well be similar to the 20 per cent. estimated above for Vauxhall's.

The position of the British Motor Corporation is in several major respects different from that of either Ford's or Vauxhall's. The latter, as the U.K. members of American groups, have no responsibility for, or investment in, the associate factories overseas. B.M.C., on the other hand, operates substantial and growing assembly and production facilities in Australia and elsewhere.

B.M.C. also is at quite a different phase of manufacturing development. Ford and Vauxhall are just reaching the end of a phase in which production has been closely concentrated round one centre. On the other hand, B.M.C. (whose principal units consist of the former Austin works at Longbridge, the Morris facilities at Oxford and Birmingham and the Fisher & Ludlow plant at Birmingham) is in the middle or later stages of a phase in which, while production is steadily increasing, all these plants are being reorganized into an integrated group.

It is probably due to the distraction caused by the rationalization process that the increase in B.M.C.'s output in units is proportionately smaller than that of Ford or Vauxhall. It seems likely that in the next two years B.M.C. will be reaping a much more ample harvest from the amalgamation than has yet been apparent. Thus, Sir Leonard Lord, the chairman, stated in his address to the shareholders last December that the standardization of components and consequent intensified manufacture had released over 1,000,000 sq. ft. of floor space, that the concentration of engine production (for all the high production models) at Longbridge had made possible a weekly output of 8,000 engines from less space than half that figure three years earlier, and that similar savings had been achieved in other mechanical components such as gear-boxes and axles. All this must obviously lead to very substantial savings in manufacturing costs. The rate of output was forecast by Sir Leonard at 10,000 vehicles a week by the late spring and this

rate has now been achieved, so that the total output for 1955 may well be 35–40 per cent. greater than for the previous year. A further increase by the middle of 1956 is envisaged, so that in the next two years the B.M.C. should achieve a rate of progress, in the increase of output and reduction of costs, similar to that of Ford and Vauxhall in the last four years.

Unfortunately, within the limitations of a short article it is impossible to discuss in similar detail the two other units among my "Big Five"—the Standard Motor Co., producing over 130,000 vehicles last year, and Humber Ltd.—the U.K. manufacturing unit of the Rootes Group. No figures have been published of the output of the Rootes Group; but the total is probably of the order of 100,000 a year, so that the grand total for the five groups is probably over 1,000,000 units, or close to 90 per cent. of the total output of cars, commercial vehicles and tractors in the U.K.

There are two important conclusions to be drawn from these figures: First, the notable reduction in costs in the last four years which has resulted from an increase in production, with the corollary that the further planned expansion of the industry seems likely to yield even greater economies, provided it is fully utilized. Second, in relation to the volume of output, the amounts of capital involved are not great; for in efficient motor car manufacture, the ratio of turnover to capital is high.[1] Thus the demand of the industry on the resources available for capital investment will not be large in relation to the potential increase in output.

II. THE DEMAND

Assuming that the expansion programme can be accomplished without difficulty, the major problem is to find buyers for the enlarged output. Any assessment of demand necessarily turns on the question of price. In the home market, price is important because the lower the price, the greater the total potential market. In the export markets, price is paramount both for competitive reasons and also because, just as in the home market, the total demand is not a fixed quantum, but is highly responsive to reduction of price.

In the early years after the war, when the world was starved of automobiles and exports from the only competing country capable of large-scale export were hampered by the

[1] For example, the turnover of Ford last year was £127 millions, for a total investment in fixed assets (at book value) of £24 millions and a net investment of less than £6 millions in trading assets.

dollar shortage, up to three-quarters of the British output of cars was exported. Even now the proportion is little short of 50 per cent.; that for tractors is nearer 80 per cent. It is not reasonable, however, to expect that quite such high ratios will continue. It is difficult to run a factory efficiently on such high ratios of export. The requirements of each market tend to be slightly different, so that motor cars made for one country are seldom suitable without modification for export to another market. Governments are prone to disrupt markets by sudden restrictions of imports. But, above all, one must expect that in the long run the motor car industry will conform to the classic pattern of the export of manufactures: namely, that the home market bears the bulk of the standing overhead costs, while exports yield the factory a price nearer the marginal cost. While it is obvious from the reports of the manufacturing companies that in the early post-war years they were able to export at prices carrying their full share of overheads, those halcyon days cannot be expected to continue for ever. Hence, the major part of standing overhead costs may have to be carried by the home market. The size of the home market must, therefore, be of paramount importance.

It is not proposed to attempt here a thoroughgoing survey of the possibilities of increased sales in the home market. But there are good reasons for thinking that the potential demand is very elastic and that, with the greatest possible reduction in costs, a considerable extension can be expected in the number of possible car owners in this country.

In September, 1952, there were more than 2½ million cars registered in this country, yet there were only about 2 million incomes in excess of £750 a year gross. It is therefore clear that the penetration of car ownership into the enormous income group between the £750 and £500 limits was already, in 1952, very considerable. The latest figures for 1955 show an increase of more than 750,000 over the corresponding period of 1952 in the number of car registrations, so that the process is obviously continuing apace.

The prodigious growth of the number of television licences current is relevant. By March, 1955, over 4½ million families had been able to afford an additional amenity which costs, in the case of the marginal customer buying a set over two years, say £35 a year. If the marginal cost of car ownership came down to, say, £60 a year, there must be a very large number of people who would buy a car as soon as they had finished paying for their television set—particularly if, as is likely, their real

incomes were steadily increasing year by year. Moreover, many of those families which have been spending for three or four years £1 to 30s. a week on instalment purchasing of furniture will, in due course, be able to divert money to buying a car—if the costs of ownership are low enough.

The proportion of cars sold in the United Kingdom by hire purchase is still quite modest. For the twelve months to March 31st, 1955, only about one in five of the new cars registered was so sold; and the proportion of used cars sold on hire purchase seems to have been little higher. In the U.S.A., by contrast, it is estimated that 50–60 per cent. of new cars, and about two-thirds of used cars, are sold on instalments. When circumstances permit, this powerful instrument has still a much greater contribution to make to the increase of sales of new and second-hand cars to the lower income group.

A substantial part of the costs of running a car in this country consists of taxation of one sort or another. If amortized over seven years, and run for 4,000 miles a year, the lowest priced car in the market costs the owner in purchase tax £18 a year, in petrol tax £15 a year and in licence fee £12 10s. 0d. a year, or about £45 in all, against a minimum of about £65 for other costs. The scope for reduction in the total costs is certainly as great in the taxation component as in the other 60 per cent. of total cost.

In short, we may conclude that hundreds of thousands of families are now within striking distance of being able to afford the ownership of a car and that a great number will become capable of doing so in the next few years, provided that the general level of incomes increases and the cost of ownership decreases.

THE EXPORT MARKET

A broad picture of the export market is given by the table opposite for the first three months of 1955. Broadly speaking, three-fifths of this market—a market of a total value at present of £400 millions a year—is to some extent protected for the British manufacturer. The main unprotected markets are the European countries (which accounted for £30·6 millions, or 30 per cent. of the total £99·9 millions) and South America (only £2·9 millions). It is in these latter markets that the competition is likely to be most severe: in Europe from Germany, France and Italy, and in South America from the same countries and from the United States.

The competitive position in these neutral markets will be determined, of course, by the suitability of the product and by price. Even if a relaxation of the world-wide dollar shortage gives greater scope than at present for the sale of American vehicles, the tendency of American passenger car design (and of course the prodigious home market entirely dominates their design policy) seems likely to make American cars—though not, of course, trucks, at all events in the larger sizes—more and more unsuitable for the greater part of the overseas markets.

The main competition in the passenger car field is likely to come from the European factories; in Germany Volkswagen, Opel (part of General Motors), Ford and Mercedes-Benz; in France Renault, Citroën and Peugeot; and in Italy Fiat. The main brunt of the battle is likely to be in the medium weight car field—the car of a weight of 18–23 cwt.—rather than in the very small car field. In the medium weight field the British manufacturers offer products which are suitable for the general requirements overseas. In the range below 18 cwt., the Volkswagen at present has a commanding position; but the Ford Anglia and Prefect seem well fitted to do battle with the Volkswagen, and so, too, will probably the new Vauxhall small car. In the still smaller class, it must be admitted, the British

U.K. Exports

	Total		To British Commonwealth, Empire and Irish Republic		
	Number	Value £'s 000	Number	Value £'s 000	Value as Proportion of Total
					%
Cars	105,792	34,053	70,258	21,565	63·3
Commercial Vehicles ..	41,237	21,626	27,650	13,365	61·7
Agricultural Tractors ..	30,721	13,403	14,724	6,124	45·7
	177,750		112,632		
Parts and Accessories..		26,008		13,799	53·1
Other Automotive Products		4,837		2,152	44·5
		99,927		57,005	57·0

industry has not yet produced vehicles which seem to offer such satisfactory solutions of the design problem as the Renault 4 C.V., and the Fiat 600; but for most of the neutral markets the demand for cars of this size is likely to be rather in the urban than the rural areas.

While the total output of German, French and Italian industries has increased in recent years relative to the British output, the British output still exceeds that of Germany by 50 per cent., of France by 75 per cent. and of Italy by 500 per cent. To a great extent the maintenance of the British lead, and therefore the success of Britain in the export markets, will depend on the relative volume of sales in the respective home markets. It seems likely that in the competing countries there is not anything like the same corpus of potential car owners so near to the threshold as in Britain—certainly not in Italy, and most probably not in either France or Germany. Provided, therefore that the potential home market in each of the four countries is developed in equal degree, British costs should remain fully competitive.

There is another important factor in the automobile export market which has not generally been appreciated outside the motor industry, in assessing what has been achieved and what can be expected in the future. While in many respects, of course, post-war conditions gave the British industry a wonderful opportunity of achieving a lion's share of the export markets, conditions were not in all ways such as to constitute an export sales manager's dream. Exports had to be achieved quickly. Not only was there no time to plan the operation as it should be planned; there was not time to train selling staff. It is not to be wondered at that in many markets all sorts of mistakes were made and all sorts of troubles laid up for the future. The manufacturers on the Continent, particularly the German manufacturers, have had time to lay their plans properly. They have had time to train their own personnel, to study the best channels of distribution, to establish the flow of spare parts. They have been able to tackle each market in turn, when they were ready for it, instead of having to try to serve all at once a whole mass of new markets. Above all, they have been able to lay their plans on the basis of selling the bulk of their output on their home market, where conditions are known and much less subject to the sudden disturbing actions of governments.

With the changed conditions which will prevail when the British manufacturers have a volume of output adequate to

meet all demands, it is to be expected that the efficiency with which the British motor car manufacturing industry will serve the export market will go on increasing. With constantly improving products, and with the lower costs which increasing volume would bring, there is more scope for expansion in the export markets than is generally realized. In the important neutral markets—the European market, and the great South American market, as and when it becomes, as it surely will, a much more important part of the world market than at present —the British industry has the possibility of getting the lion's share. But this depends above all on the volume sold in the home markets.

III. THE ECONOMIC IMPLICATIONS

It appears from what has been said above that two important features are characteristic of the present stage of development of the British automobile industry: First, that unit costs of production are, to an unusual degree, influenced by volume, so that an increase in the output will lead to a notable reduction of costs. Second, that the total demand for automobiles, both at home and abroad, is unusually elastic. It would, for example, not be unreasonable to argue that a reduction of 25 per cent. in the cost of owning and running a motor car in this country might *double* the number of families who would find it worth while to do so, and similarly in the export markets.

Now if motoring is an activity for which both the demand and supply have these unusual characteristics, there is an important deduction to be made. It is this: If any burden, such as taxation, increases the price to the consumer of that activity, the reduction in consumption will be much greater than if the opposite conditions prevailed.

It is, indeed, only another way of stating these propositions to say that any factor which raises the price of the product will cause a relatively large fall in demand, that the shrinkage in output will raise unit costs and the price to the consumer be raised therefore by more than the amount of the tax. Hence the raising of a given quantum of revenue by taxing such an activity as motoring is likely to have a much greater effect in distorting the pattern of economic activity and frustrating the potential growth in the wealth of the country, than raising the same amount of revenue by the taxation of other activities. There will be a greater destruction of potential wealth by the extinction of a very big amount of potential consumer surplus.

If this argument is accepted, it follows that the policy of successive governments in this country over the last 50 years has been open to grave objections: that it would have been wiser to raise the sums which have been raised by the taxation of motoring by some other form of taxation, such as, for example, a general sales tax. It would be easy to make a strong case for saying that the excessive taxation of motoring between the wars did prodigious harm to our economic life. If motoring had been encouraged in every way, instead of being discouraged by excessive taxation and by restricted road development, it could be argued that our whole economy would have been greatly strengthened.

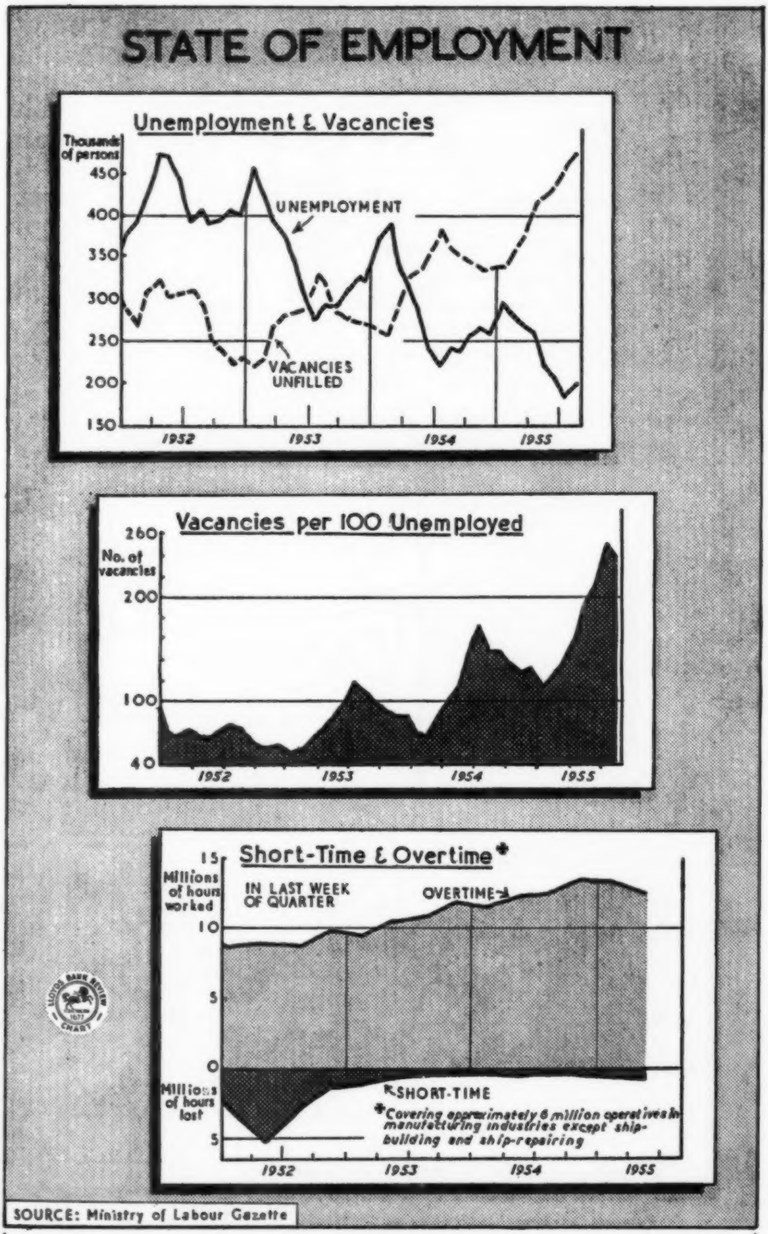
As far as the years since the war are concerned, it could not, of course, be maintained that the excessive taxation of motoring has had much effect in restricting the growth of production. The reason is, of course, that pretty well throughout the period the production of automobiles in this country has never been sufficient to meet the demand. Thus, the principal effect of excessive taxation has been to mop up surplus purchasing power.

It would doubtless be difficult to argue that the objections to excessive taxation of motoring on the grounds of general principle, indicated above, provide a solid case for reducing such taxation immediately. On the other hand, they do provide an exceedingly strong case for a sharp reduction in taxation as soon as the demand for motor cars in this country has caught up with the available supply.

It is open to argument how much further the State should go in directing our economic activity. But if the view is taken that the responsibility of the State should be limited to the broadest economic decisions, and that within those limits the direction of resources should be left to the free play of economic forces, the corollary is that the State must see to it that in fact the economic forces do have free play. A great growth of the motor car manufacturing industry can yield a most bountiful harvest, of reducing costs, of expanding exports and of consumers' satisfaction—a real enrichment of the lives of ordinary men and women. The free play of economic forces would tend to bring about this exuberant growth. But it can only too easily be stunted by excessive taxation. The amount at stake on this decision is great.

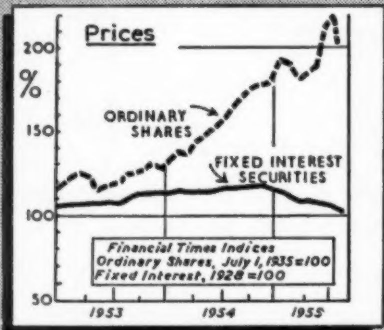
G. WANSBROUGH.

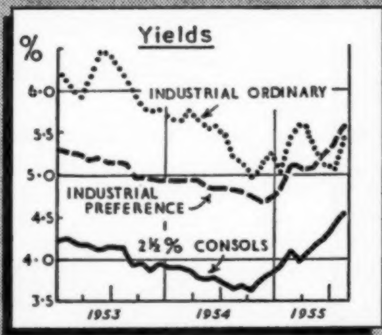
London.
August, 1955.

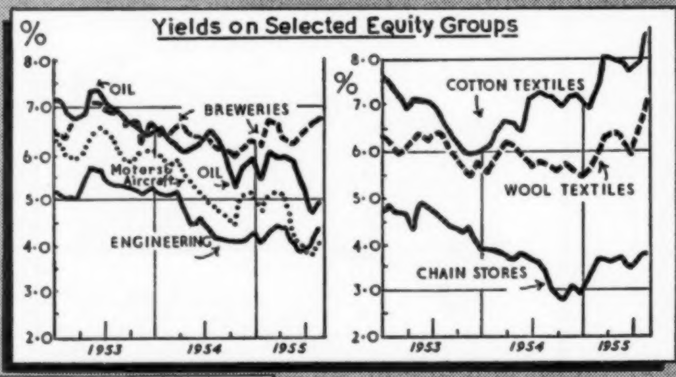


Since June, jobs vacant have been more than double the number of workers registered as unemployed. The pressure on the labour market is also evident from the considerable amount of overtime worked over the past year.

SECURITY PRICES & YIELDS



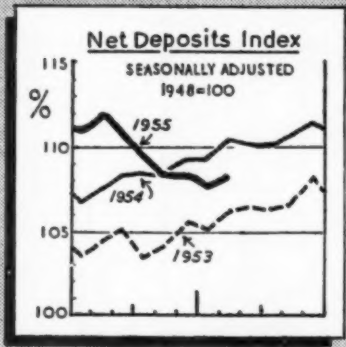


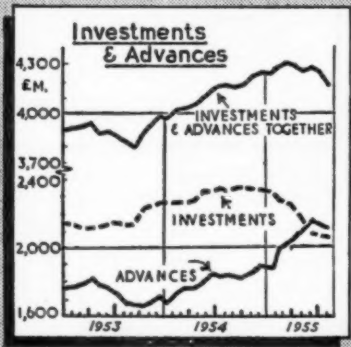


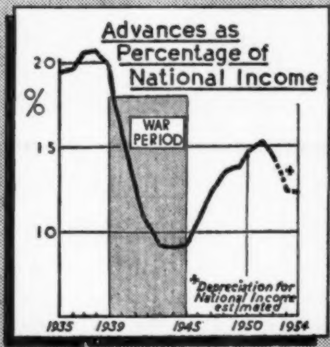
SOURCES: Financial Times
The Actuaries' Investment Index

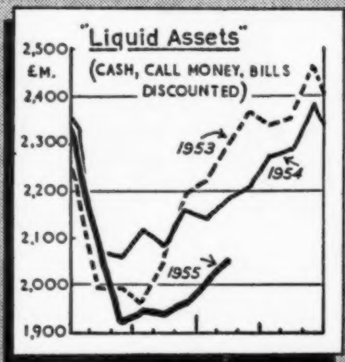
Fixed interest securities have been under pressure for some months, the yield on Consols having risen from 3·6 per cent. last October to 4½ per cent. in August. On the other hand, industrial ordinary shares advanced to reach a new peak in July, but have since reacted sharply.

CLEARING BANKS



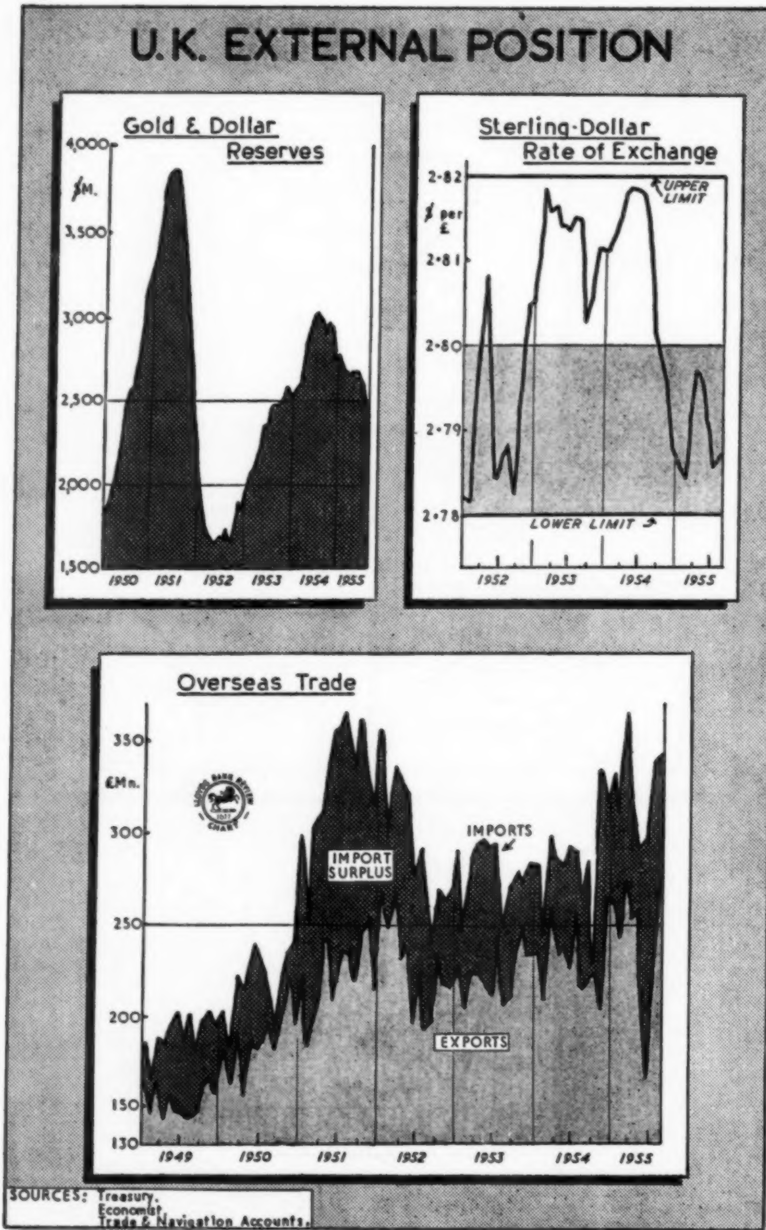




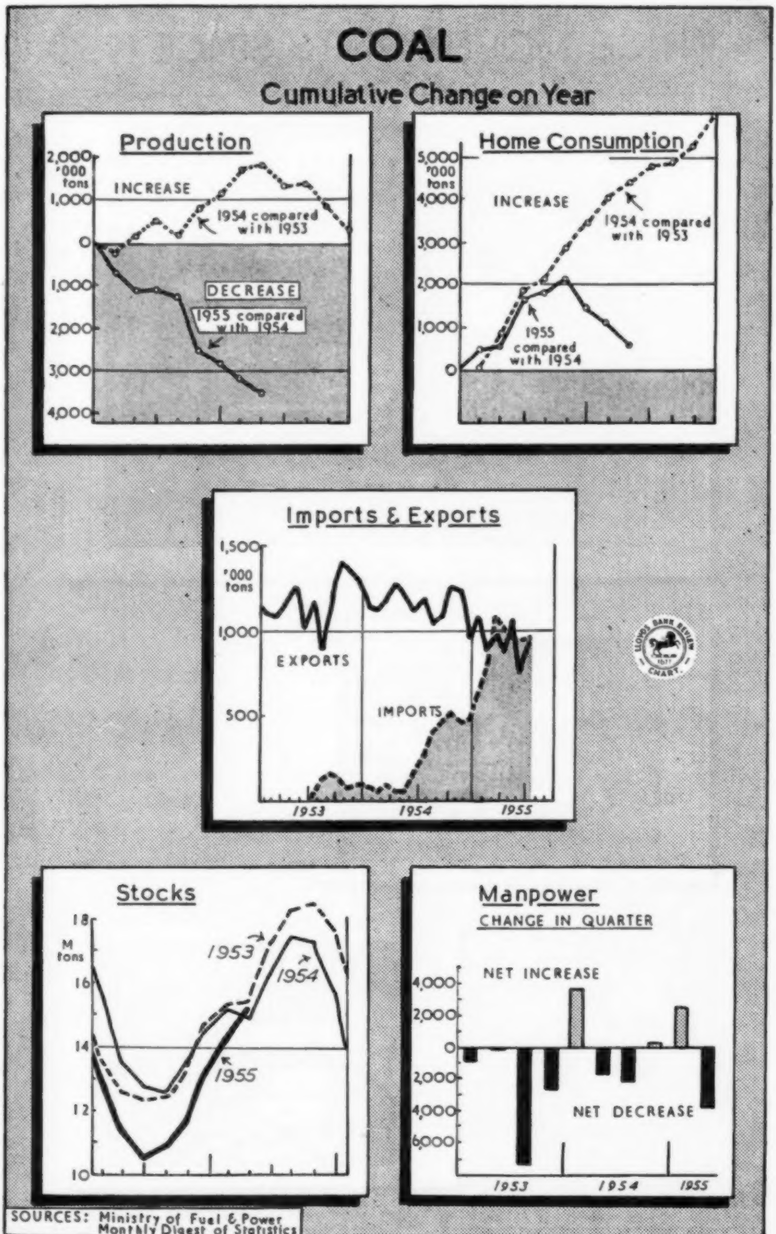


SOURCES: Committee of London Clearing Bankers
National Income publications

Lloyds Bank index of net deposits (seasonally adjusted) showed a net fall of nearly four points between the February peak and August, compared with a rise of over 2½ points in the same months last year. Until the recent contraction bank advances showed a strong upward trend but in relation to national income are very much lower than pre-war.



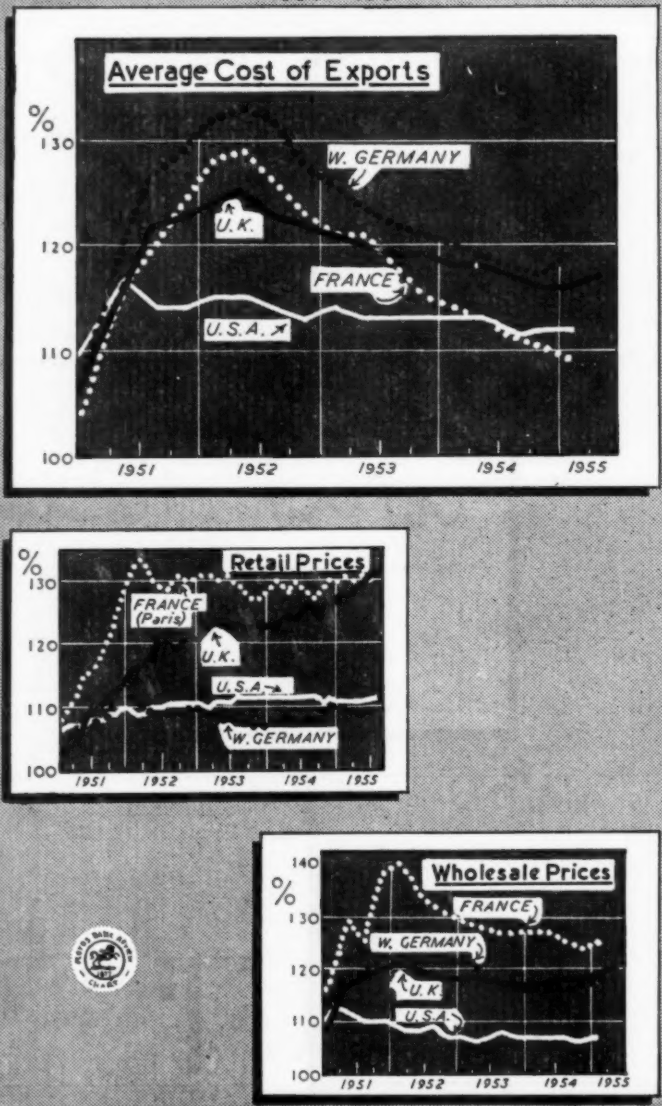
In the ten months to the end of August our gold and dollar reserves fell by \$479 millions, against a fall of \$2,205 millions in the ten months of the 1951/2 crisis. The merchandise trade figures are still being affected by the transport strikes earlier this year.



Production to the end of August was about 3½ million tons less than in the same months of 1954, while home consumption was up by over half a million tons. In the same period, although exports and imports in tonnage were about equal, we were a net importer of coal to the extent of £15 millions, whereas in the corresponding months of 1954 exports exceeded imports by £33 millions.

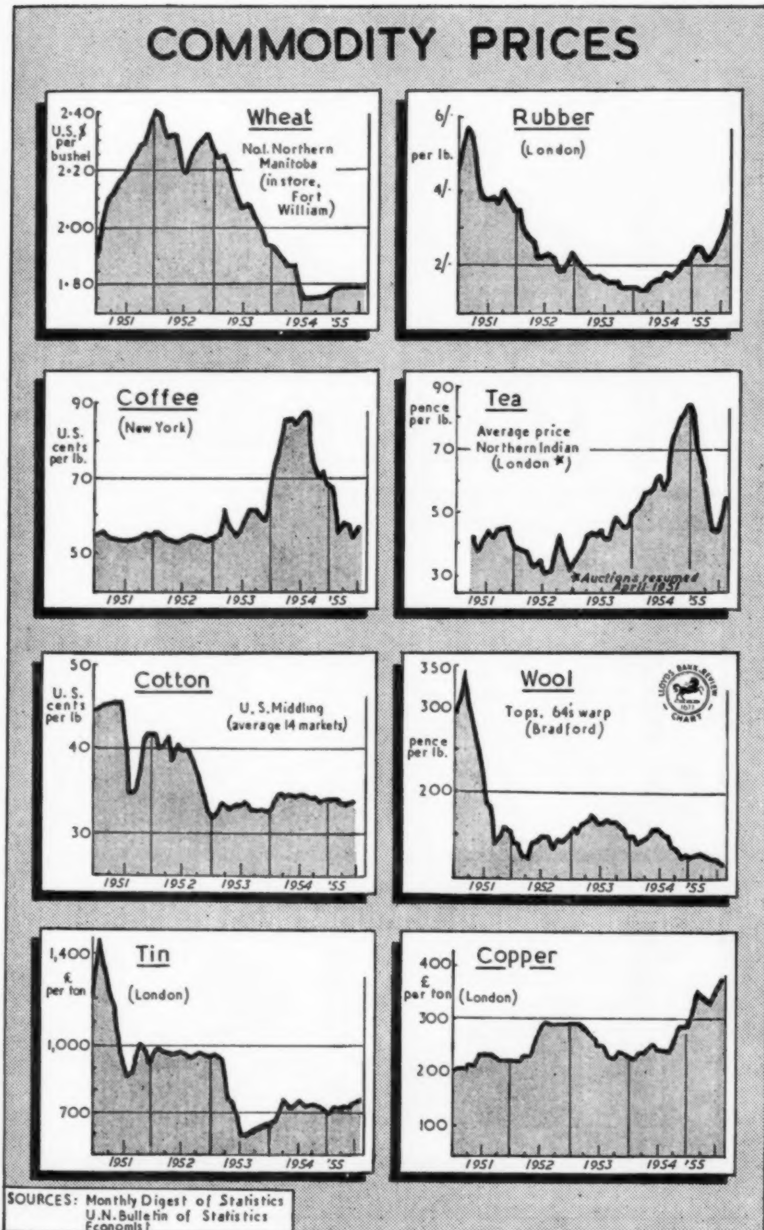
PRICE MOVEMENTS SINCE 1950

1950 = 100



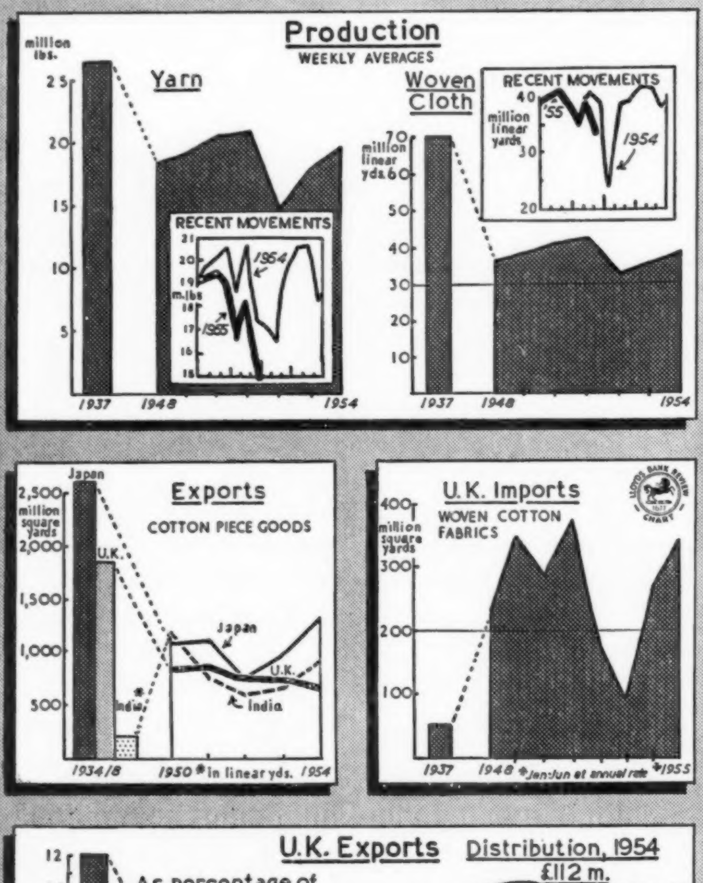
SOURCE: O.E.E.C. Statistical Bulletin

Since 1950 our competitive position (as measured by export prices) has deteriorated somewhat compared with the U.S.A. but has been fully maintained by comparison with W. Germany. U.K. retail prices have risen appreciably since 1952; in the other countries shown there has been relatively little change.



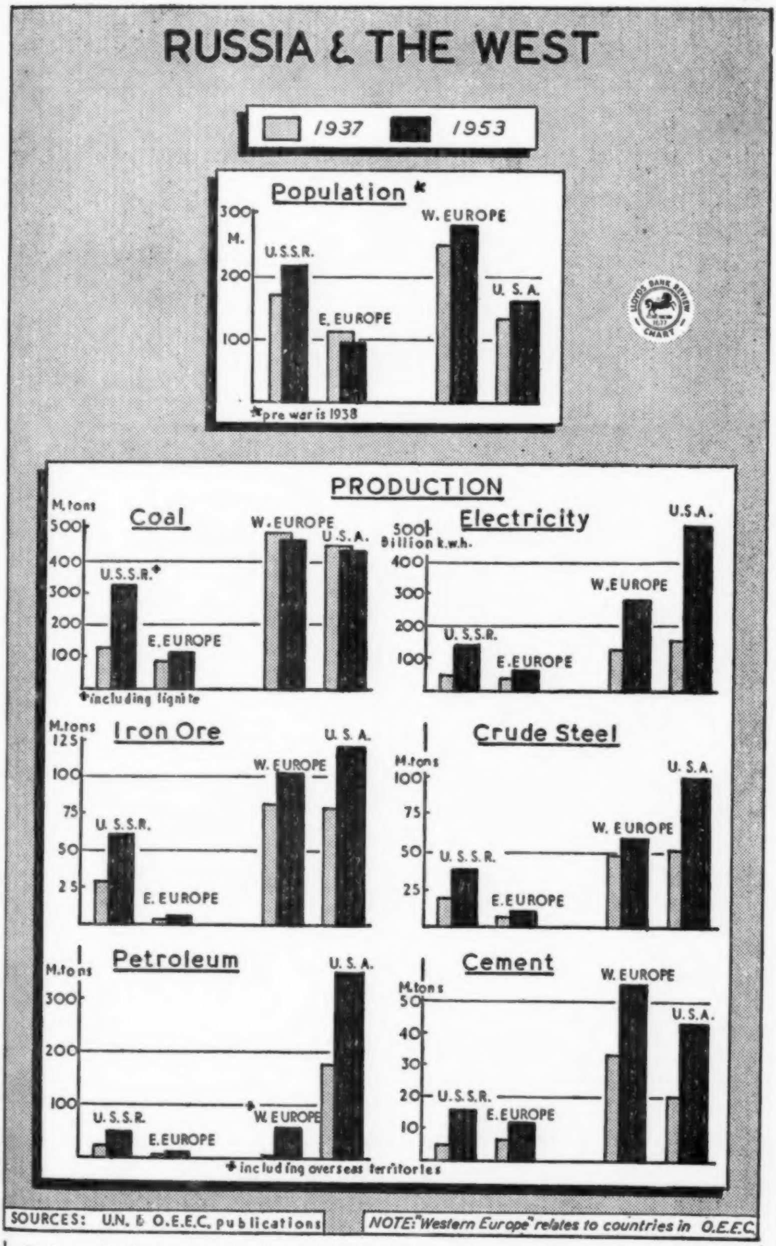
Rubber and copper prices have recently been particularly buoyant, while coffee and tea prices remain well below last year's peak levels. Prices of the other commodities charted above have shown little movement over the past year or so.

COTTON



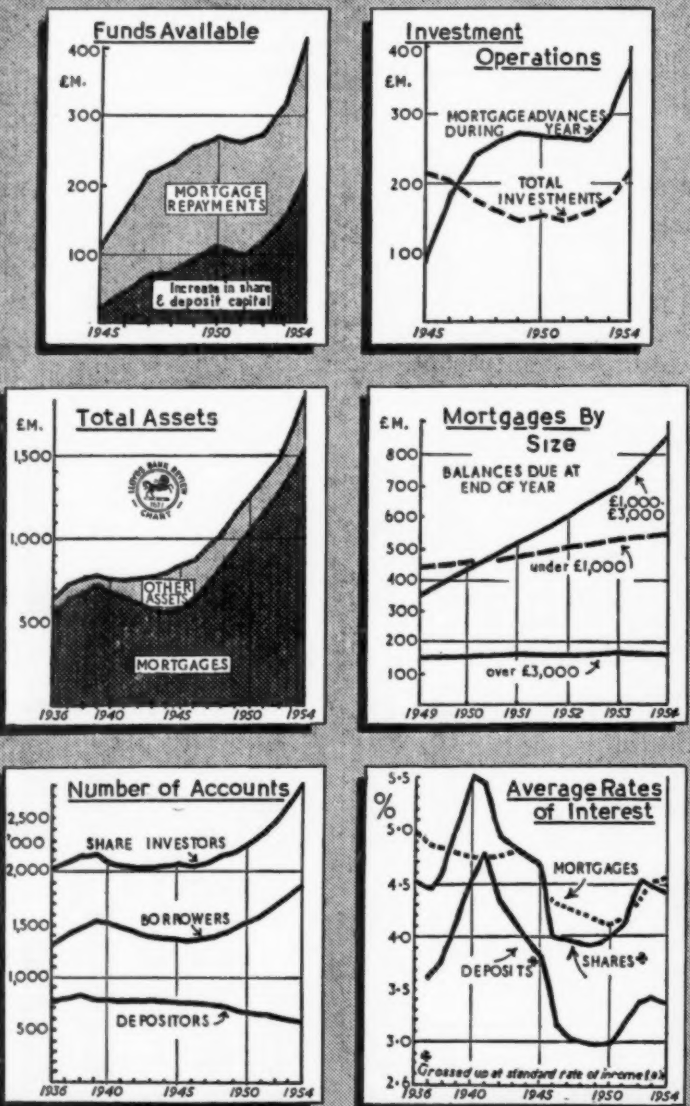
SOURCES: Annual Abstract of Statistics
Trade & Navigation Accounts
Commonwealth Economic Committee

Cotton production so far this year has been running below the 1954 level. Exports have also fallen off somewhat and form a dwindling share of total exports. Imports of cotton fabrics, in contrast, have risen appreciably, the rate in the first half of the year being nearly up to the 1951 peak.



In heavy industry, production in W. Europe and the U.S.A. still far exceeds that in the U.S.S.R. and E. Europe. In some cases, however, the rate of increase in Russian production, compared with pre-war, seems to have been greater than in the West. In coal, indeed, output has more than doubled, while production in W. Europe and the U.S.A. has fallen slightly.

BUILDING SOCIETIES



SOURCES: Registrar of Friendly Societies Reports
Building Societies Year Book

Building society totals have expanded rapidly in recent years. With nearly 3 million share investors in 1954, total assets exceeded £1,800 millions, of which 84 per cent. was in mortgages.

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